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THE EMERGENCE OF ECONOMIC TRADING BLOCS: THE ROLE OF JAPAN AND THE IMPLICATIONS FOR LATIN AMERICA

by

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Submitted in partial fulfillment of the
requirements for the degree of

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ABSTRACT

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TABLE OF CONTENTS

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EXECUTIVE SUMMARY

Since the end of the Cold War global international economic relationships have become even more important. Economically, Japan has been viewed as an aggressive adversary vice a competent competitor. Due to the long historic economic relationship of the United States and Latin America there has been concern over Japan's aggressive economic practices in the Latin American region.

In one form or another Free Trade Areas have been in existence since World War II. With the past failures of the General Agreement on Tariffs and Trade (GATT) to resolve trade issues, regional economic trading blocs have emerged as the wave of the future. Although Japan's economic involvement in Latin America dates back to pre-World War II, it is the current economic strategies that are of interest. This thesis is intended to determine what Japan's strategy is for the Latin American region and what influence it has on the economic development of the region.

The three competing hypothesis presented suggest that Japan's interest in Latin America is driven by different factors including the large immigration of Japanese to the region after World War II, the basic needs for raw materials and the need to play an economic role in any developing economic bloc. In the pivotal section of this thesis the

economic relationships and trade patterns of Japan's activities in Latin America are compared to those instituted by Japan in Southeast Asia. I argue that Japan does have a strategy for targeted Latin American countries that is situational for the economic needs of Japan; additionally, economic activities are approached on a case by case basis. Each country is approached with an astute economic policy nuanced by the economic goals and needs of Japan i.e., the need of raw materials and/or solidifying substantial trade positions in a potential Western Hemisphere trading bloc.

In conclusion, the implications of both the emergence of trading blocs and the new-found mission of Japan in Latin America opens up endless possibilities of trade patterns in the Pacific Rim. With the recent advances with GATT and the regional trade agreements resulting in more free trade opportunities, the Latin American region can only benefit with economic growth and development that will contribute to a chain reaction of economic stimuli around the Pacific Rim.

I. INTRODUCTION

A. THE NEW REALITIES

Since the end of the Cold War more attention has been given to the emergence of Japan as an economic superpower. With the highly publicized controversial Japanese trade practices there has been a growing view in the United States of Japan as an adversary. This rivalry continues as Japan secures stronger economic influence in the Latin American region. With the potential of emerging trading blocs the Japanese have increased economic activity in the Latin American region in the past few years.

Recently more attention has been given to the emergence of these regional economic trading blocs. With the past highly publicized problems with the General Agreement on Tariffs and Trade (GATT), there has been a growing view that economic regionalism is the wave of the future.

Since the late 1950's the European Community (EC) has had significant economic influence as it has evolved into a powerful economic trading bloc of the 1990's. The United States and Canada have had a significant free trade agreement dating back to the Reciprocity Treaty of 1874 and more

recently with the Canada-U.S. free trade agreement.[1] Since Canada and Mexico already conduct approximately two-thirds of their trade with the United States the addition of Mexico and the establishment of the North American Free Trade Area (NAFTA) will give legitimate birth to the second major economic trading bloc. The third free trade area is Southeast Asia led by the economic dynamics of Japan.

The history of Japanese economic influence in Latin America dates back to World War II; however, there continues to be increasing and diversified economic activities in the region in the past few years. The question is : What is Japan's economic strategy for Latin America and why?

The purpose of this thesis is to determine what is Japan's economic strategy for Latin America. In determining what drives Japan to Latin America, I propose three competing hypotheses:

1. Japan's interest in Latin America is based on the post World War II Japanese immigration to the region.

2. Japan's interest in Latin America stems from the basic geo-strategic economic needs of commercial gain and raw material resources.

3. Japan's interest in Latin America is driven by the economic necessity of being a part of any emerging economic trading bloc.

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[1] "US and Canada Trade Agreement," <u>1987 Congressional Quarterly Almanac</u>, v. 3, p. 662, 1987

B. METHODOLOGY

Associational analysis is used to link Japanese economic relationships and patterns to the economic development of the Latin America region; as well as, to identify those links that are most likely to influence future economic events in Latin America. There is a tendency to view Japan's aggressive economic practices as adversarial behavior vice calculated and situational competition. This analysis provides an approach to identify indirect as well as direct links to economic relationships in previous regions of Japanese economic development and apply them to various causal chains in Latin America.

The four major sections of the thesis will be 1) the evaluation of Japanese influence during the three economic development phases in Latin America. This section will provide the basic information to set the stage of Japan's awakening to the economic and political dynamics in Latin America; 2) the formation of regional economic blocs and current strategic economic activities in the region; 3) this section focuses on Japanese economic activities and strategies used in Southeast Asia compared to current business practices in the Latin American region; and 4) country case studies of the economic dimensions of the Japanese influence. The countries selected showcase Japanese economic influence in four distinct and different relationships: Panama as a tax shelter and shipping haven, Mexico as a cooperative growth oriented economy,

Brazil as a defiant nation groping with financial problems, and Chile carving out its place in a new world order.

II. MARKET MENTALITY

A. THE JAPANESE PHOENIX 1952-1976

Upon regaining its independence in 1952, Japan rose out of the ashes emerging as an economic entity. Shortly after World War II large numbers of immigrants from Japan relocated to Latin America with over 100,000 settling in Brazil, 80,000 in Peru and another 30,000 in Argentina. The government of Japan understood the economic importance of these ethnic enclaves as well as the limitations of the island. The economic importance of establishing an import source for raw materials and food was paramount. Japan looked toward Latin America, using the Japanese communities in various countries to facilitate the trading relationships.[2]

From the 1960's to mid 1970's Latin America was in a fast development mode through import substitution industries, protective import barriers and debt financed growth. Japan was attracted to the region not only as a source of raw materials but also as a source of trade for their own rapidly developing economy.

Since 1952 the policies of Japan toward Latin America have been in concert with its most important relationship- the

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[2] Pope G. Atkins, Latin America in the International Political System, (Westview Press, 1989) p. 104.

United States. Japan was content with the United States influence over Latin America which was perceived as a deterrence to the spread of communism and a global balance of power. Taking the lead of American investors Japanese trading companies made major investments in Latin America expecting tidy profits as the Americans had been receiving. It is a question of whether supply or demand factors caused the competitive lending by Japanese banks that began in the 1970's and continued until 1982. By 1982, seven countries accounted for two thirds of all bank loans to the Third World with Latin America the most important borrowing region. Brazil and Mexico alone represented 43% of Third World debt while Argentina, Venezuela and Chile added another 14% [3] The causes of the lending wave are debatable; however, both sides had their reasons. On the supply side- the Japanese banks had high liquidity and perceived profit margins that resulted in "loan pushing" by the government of Japan.[4] On the demand side- the Latin American governments borrowed to promote industrialization developing economic growth to aid their own legitimacy.

The timing of the Japanese loans caused problems as well. As illustrated in Table 1 from 1970-1982 the U.S. banks

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[3]Barbara Stallings, "The Reluctant Giant: Japan and the Latin American Debt Crisis," Journal of Latin American Studies, v. 22, February 1990, p. 3.

[4]Stallings, p. 2.

managed an average of 42% of the Latin American loans, while Japanese banks were far behind with only 10%. U.S. loans were consistent while Japanese banks by contrast, operated in cycles as the oil shocks affected the Japanese economy causing banks to back off until there were more favorable conditions.[5] Although the U.S. had twice the share of Latin American total debt, Japanese exposure was higher at 72% of total late developing country (LDC) loans.[6] Since Japanese banks have a lower capital to asset ratio it makes the loans to Latin America more important in terms of bank vulnerability. By mid-late 1970's Japan had substantial investments in natural resources in Mexico and Brazil. Japan's imports from Latin America concentrated in minerals, fuel (oil) and agriculture; whereas, exports to Latin America were industrial products (that supported the stagnating import substitution industries) and some consumer goods.

B. THE AWAKENING 1976-1982

1976 saw Jimmy Carter elected to the White House. Without notice and almost immediately upon taking office the Carter administration changed policy toward Latin America drastically, including curbing business practices of U.S. firms in the region. Japan now started to realize that it

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[5] Stallings, p. 5.

[6] Stallings, p. 7.

TABLE 2-1. LEAD MANAGERS FOR LATIN AMERICAN EUROLOANS, 1970-82 (MILLIONS OF DOLLARS). FIGURES IN BRACKETS REFER TO PERCENTAGES OF ANNUAL TOTAL

Year	United States	Japan	Other	Total
1970	55.5	0	153.2	208.7
	(26.6)	(0)	(73.4)	(100.0)
1971	462.9	0	323.0	785.9
	(58.9)	(0)	(41.1)	(100.0)
1972	972.5	251.2	750.7	1,974.4
	(49.3)	(12.7)	(38.0)	(100.0)
1973	1,931.6	318.1	1,198.9	3,448.6
	(56.0)	(9.2)	(34.8)	(100.0)
1974	2,677.6	112.4	1,757.5	4,547.5
	(58.9)	(2.5)	(38.6)	(100.0)
1975	3,591.9	0	2,379.9	5,971.6
	(60.1)	(0)	(39.9)	(100.0)
1976	4,636.9	90.0	4,046.8	8,773.7
	(52.8)	(1.0)	(46.1)	(100.0)
1977	4,931.8	384.1	3,858.7	9,174.6
	(53.8)	(4.2)	(42.0)	(100.0)
1978	7,640.2	2,667.5	7,178.4	17,486.1
	(43.7)	(15.3)	(41.0)	(100.0)
1979	9,147.8	2,510.7	12,226.6	23,885.1
	(38.3)	(10.5)	(51.2)	(100.0)
1980	6,795.8	580.2	11,360.1	18,736.1
	(36.3)	(3.1)	(60.6)	(100.0)
1981	7,545.9	3,233.9	10,779.9	21,559.9
	(35.0)	(15.0)	(50.0)	(100.0)
1982	7,396.3	3,169.8	10,566.2	21,132.3
	(35.0)	(15.0)	(50.0)	(100.0)
Total	57,786.7	13,317.9	66,599.7	137,704.3
	(42.0)	(9.7)	(48.4)	(100.0)

Source: Barbara Stallings, "The Reluctant Giant: Japan and The Latin American Debt Crisis," Journal of Latin American Studies, Volume 22, February 1990

must start making its own decisions and policies. During the late 1970's there was a loss of Latin American economic momentum caused by the protective import barriers, debt financed growth, and stagnated industry. With the onset of the debt problem voluntary lending ceased. Third world debt had increased from $11 billion in 1970 to $261 billion by 1982 with Brazil and Mexico alone making up 43% of the total.[7] Latin America became less attractive for Japanese investment and there was a shift of Japanese interest to other areas of the world (southeast and south Asia). In 1973 there were three major U.S. decision policies with international impact that suddenly made the government of Japan aware of the strategic importance of the Latin American region:[8]

1. The renegotiation of the Panama Canal Treaty caused Japan great concern because of the dependence on the canal for Japanese ships to get to European and other markets.

2. The embargo on the export of soybeans from the United States forced Japan to look for another source which Brazil was able to provide.

3. The U.S. decision to develop Alaskan oil for domestic use caused Japan (absolutely certain they would have access to this oil) to pursue development of Mexican oil resources.

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[7]Stallings, p. 3.

[8]Susan Kaufman Purcell and Robert M. Immerman, "Japan, Latin America, and the United States: Prospects for Cooperation and Conflict," Japan and Latin America in the New Global Order, (American Society Lynne Rienner Publishers, 1992), p. 124.

These factors contributed to Japan's emergence with a new self determination on international policy versus the unchallenged support of U.S. policy as in the past. Some of the strong stances Japan has taken against United States policy in Latin America include:

- opposed U.S. military intervention in the region
- defied U.S. embargo and became the principal purchaser of Cuban sugar
- supported pro-Argentine position on Malvinas conflict

By late 1988 Japan had spread her wings in the political arena of Latin America.

C. THE DEBT CRISIS 1982-1988

Some of this new-found Japanese self-determination toward decision making and policy setting was evident when the Japanese investors got caught in the debt crisis. There was immediate criticism of the U.S. investment policies toward Latin America and the region's debt management. The debt crisis was partly caused by over borrowing and the mismanagement of import substitution industries.[9] Mexico, in 1982, was the first to default on loans and was quickly followed by other counties unable to pay the debt service.

To understand Japan's involvement in the debt crisis resolution sets the stage to understanding Japan's redefined

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[9] A. Blake Friscia, "Japanese Economic Relations with Latin America," Japan and Latin America in the New Global Order, (Lynne Rienner Publishers, 1992), p. 9.

interest in Latin America in the post crisis period. Although several plans were devised, the Brady Plan (a plan for linking bank loan increases to economic growth and structural reforms) was initiated and applied toward Mexico with some positive results. Although Japan was lured into supplying more money under the Brady Plan to Latin America in debt resolution projects, the government of Japan was also developing another plan to increase its own role in Latin American affairs.

Japan's own initiative, in 1988, known as the "Capital Recycling Program" would have interesting consequences on U.S. economic foreign policy and the future development of Latin America. The stated purpose of this plan was to direct part of Japan's large trade surplus to Latin America as official assistance and loans. The Japanese presented the plan as a way to use its new wealth as strategic assistance to help solve problems threatening U.S. interests and economic stability. Japan's Minister of Finance- Tadao Chino states "foreign investment should contribute to the government's foreign policy goals and strengthen Japan's economy".[10] Despite rhetoric to the contrary, this statement clearly signals Japan's objective of enhancing its economy abroad and also its foreign policy. It could be better understood as an investment for the future of Japan in Latin America.

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[10]Friscia, p. 63.

Although Japan had developed the Capital Recycling Plan as a concept to transfer excess capital to developing countries with the focus on the benefit to the Japanese economy, the concept was heralded as one of Japan's few major international initiatives in the post- World War II era.

The funds would be channeled through various Japanese organizations designating Japanese investment handlers as the money managers. Some of agencies controlling the money movement included:

* Direct loans by the Japanese Export/Import Bank (JEXIM)
* Joint or co-financing schemes with other international banking systems
* Assistance credited as Japanese foreign aid using such agencies as the Overseas Economic Cooperation Fund (OECF)
* Capital Recycling funds as financial contributions to the International Monetary Fund (IMF) and the World Bank.

Approximately 45% of the monies the Japanese had designated as Capital Recycling Plan funds were direct contributions to the IMF. This caused concern to the Japanese because they lost control of how the monies would be utilized; whereas, concessional development loans arranged through Japanese agencies were more lucrative and more of what the Japanese had in mind.

The types of loans promoted by the Japanese in their investments were designed to secure a commitment from the developing country that would promote Japanese economic interests and benefit Japanese trade and investments in the future.

Although prior to 1980 Brazil was the third ranking country for Japanese investments abroad (specifics discussed in Brazil case study), by mid-1980's the chief foreign direct investments were still only for tax haven purposes and shipping (specifics discussed in Panama/Caymen case study). In fact, by 1988 Caribbean investments had increased 800% from $640 million in 1981 to 5 billion (Table 2).[11] The majority of this was due to the establishment of the Japanese Export/Import Bank to handle the Capital Recycling Plan funds. The investment statistics are misleading because it's only paper investments for Japanese tax purposes instead of actual manufacturing investments for economic growth in the region. In fact, the whole setup for the Capital Recycling Plan proved to be a disappointment to the Latin American region with only 22% being offered to Latin America and over 50% being funneled to Southeast Asia developing countries.[12] The situation has changed through the years. As of 1992 the regional commitment of the Export-Import Bank still favors Asia as indicated in Table 2-3.

[11]Purcell, p. 19.

[12]Stallings, p. 24.

TABLE 2-2

	1988		1989		1990		Cumulative April 1951–March 1991	
	Amount	%	Amount	%	Amount	%	Amount	%
Brazil	510	1.1	349	0.5	615	1.1	6,560	2.1
Mexico	87	0.2	36	0.1	168	0.3	1,874	0.5
Argentina	24	0.1	3	0.0	213	0.4	431	0.1
Venezuela	51	0.1	75	0.1	77	0.1	341	0.1
Chile	46	0.1	47	0.1	30	0.1	311	0.1
Peru	0	0	0	0	0	0	696	0.2
Subtotal	718	1.5	510	0.8	1,103	2.0	10,203	3.3
Panama	1.712	3.6	2,044	3.0	1,342	2.4	16,244	5.2
Cayman Is.	2,609	5.5	1,658	2.5	588	1.0	7,332	2.4
Bahamas	737	1.6	620	0.9	121	0.2	3,459	1.1
Subtotal	5,058	10.8	4,322	6.4	2,051	3.6	27,035	8.7
Other Lat. Am.	652	1.4	396	0.6	474	0.8	3,245	1.0
Total Lat. Am.	6,428	13.7	5,238	7.8	3,628	6.4	40,483	13.0
U.S.	21,701	46.2	32,540	48.2	26,128	45.9	130,529	42.0
Europe	9,116	19.4	14,808	21.9	14,290	25.1	59,265	19.0
Asia	5,569	11.8	8,238	12.2	7,054	12.4	47,519	15.3
Other	4,208	8.9	6,716	9.9	5,811	10.2	33,012	10.7
World	47,022	100.0	67,540	100.0	56,911	100.0	310,808	100.0

Source: A Blake Friscia, "Japanese Economic Relations with Latin America" Japan and Latin America in the New Global Order, 1992

TABLE 2-3

Regional Commitments by Export-Import Bank (as of 3/92)

Region	Amount(mill U.S. $)	Percent share
Latin America-Caribbean	5,292	29
Asia	6,706	37
Europe, Africa, Middle East	3,114	17
IMF-structural lending	3,040	17
total	18,152	100

Source: Japan Ministry of Foreign Affairs and Export-Import Bank of Japan 1992

D. NEW GLOBAL PARTNERSHIP

President Bush took office in 1989 giving Japan new hope for harmony in policies toward Latin America. Since the Cold War is over the U.S. policy toward Latin America has not been as security oriented and there has been a stronger focus on promoting economic growth in the Latin American region. These changes include an adoption of freer trade and investment policies toward the region. There has also been U.S.-Japanese cooperation to support democratic governments and economic reforms. Japan fully supported President Bush's radical shift from world-wide aid to a policy of trade and investment. This approach is more in concert with the Japanese attitude that self-help efforts can be better motivated by repayment obligations.

However, Japan has not been without its own money problems. Japanese banks had a serious crisis in 1990 with

major cashflow problems and investment justification problems with the government.[13] This caused tighter regulations for foreign investment approved by the government of Japan.

By 1980 Japan had significant imports from Brazil, Mexico and Chile; industrial operations in Brazil and Mexico; and technical assistance contracted in Brazil, Peru and Paraguay; but by 1990 the declining shares of import/export business with the region was dramatic. Total shares of Japanese exports to Latin America had dropped from 6.9% in 1981 to 4.1% by 1991. Although the Japanese share of imports from Latin America (with a focus on raw materials,fuel and food) had increased by 47.5% in dollars, the share percent actually dropped from 4.7% in 1981 to 4.2% by 1991.[14]

The evolution of Japanese trade with Latin America from 1981-1991 is shown in Table 2-4.

Japan's concentration had shifted to southeast Asia nurturing their high tech industry with less risky return on investments. Even so, Japan's importance as an export market is significant to several Latin American countries by percent of total exports with Chile at 21%, Peru at 12%, Honduras at 11% and Brazil at 10% (Table 2-5a). Conversely, on the percent of total imports the importance of Japan ranges from

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[13]"Japanese Banks: From Bad to Worse," The Economist, 7 November 1992

[14]Friscia, p. 11.

TABLE 2-4

	Total Exports	Exports to L.A.	L.A. Share %	Total Imports	Imports from L.A.	L.A. Share %	L.A. Balance
1981	152.030	10.516	6.9	143.290	6.669	4.7	3.857
1982	138.331	9.086	6.5	131.931	6.268	4.8	2.818
1983	146.927	6.391	4.3	126.393	6.462	5.1	-71
1984	170.114	8.549	5.0	136.503	7.230	5.3	1.319
1985	175.638	8.486	4.8	129.539	6.242	4.8	2.244
1986	209.151	9,494	4.5	126.408	6.194	4.9	3.300
1987	229.221	8.760	3.8	149.515	6.355	4.3	2.405
1988	269.917	9.297	3.4	187.354	8.313	4.4	984
1989	274.175	9.381	3.4	210.847	8.870	4.2	511
1990	286.948	10.279	3.6	234.797	9.351	4.2	428
1991	314.525	12.793	4.1	236.737	9.838	4.2	2.955
% Change 1981-1991	106.9	21.6		65.2	47.5		

Source: A. Blake Friscia, "Japanese Economic Relations with Latin America," Japan and Latin America in the New Global Order, 1992

the Bahamas at 16% to Venezuela and Costa Rica both at approximately 3.3% (Table 2-5b).[15]

In the new Japanese flexing of political muscle associated with financial aid to foreign countries, new conditions now applied to potential aid recipients in Latin America. Some of the regulations for aid are less than congenial to U.S. policy:

1. no aid for political reasons;
2. review of percentage of aid used for military purposes;
3. restrictions on the amount of weapons sold;
4. no aid if in possession of weapons of mass destruction;

[15]Friscia, p. 15.

TABLE 2-5a

Relative Importance of Japanese Exports to Latin American Countries, 1991 (eleven leading exporters)

	Exports to Japan (million U.S.$)	Japan % Share of Country's Exports
Chile	1,888	21.1
Peru	395	11.9
Honduras	103	11.2
Brazil	3,180	10.1
Guyana	18	7.2
Mexico	1,741	6.2
Argentina	603	5.0
Ecuador	107	3.7
Colombia	274	3.6
Venezuela	468	3.0
Guatemala	47	2.6

TABLE 2-5b

	Imports from Japan (million U.S.$)	Japan % Share of Country's Imports
Bahamas	385	16.0
Colombia	495	10.5
Ecuador	193	8.7
Paraguay	147	8.7
Chile	631	8.6
Mexico	2,317	7.4
Argentina	448	6.1
Brazil	1,226	5.8
Dominican Republic	104	4.9
Venezuela	529	3.7
Costa Rica	78	3.3

Source: A. Blake Friscia, "Japanese Economic Relations with Latin America" Japan and Latin America in the New World Order, 1992

5. and recipient must be actively pursuing human rights, democratization and a free economy.

Japan had also become politically involved in Central America by sending observers for elections to El Salvador, Nicaragua and Haiti not to mention the democratization requirement to receive aid.

From the Latin American point of view this is a real catch-22 in that the procyclical behavior of direct foreign investment implies that a rise in direct foreign investment has to be preceded by the reestablishment of an overall economic and political climate conducive to growth, which in turn requires a solution to the debt problem.[16]

Regardless of all the setbacks, by 1991 the long awaited economic revival of Latin America began with moves toward democratic governments and economic policies designed to slash inflation.[17] The big five debtor nations of Brazil, Mexico, Argentina, Venezuela and Chile have had successful bond sales. Additionally, Mexico, Venezuela and Chile have rising value of debt on the secondary markets.[18] Most Latin American debt

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[16]Eva Paus, "Direct Foreign Investment and Economic Development in Latin America: Perspectives for the Future," Journal of Latin American Studies, v. 22, May 1989, p. 231.

[17]"Virtue Rewarded," The Economist, 31 October 1992.

[18]"There is a Better Way, and They Have Found It," The Economist, 19 October 1991, p. 21.

is being sold to rich Latin Americans who use it as a way to repatriate flight capital or to recycle drug money.[19]

The future prospects are interesting since the Japanese have a new found mission to support development in the third world. An increased Japanese presence is evident with foreign investments to Mexico, Brazil (conditional), Chile and Venezuela. Japan will continue its reverse export programs, assembly industries and searches for access to American markets. The region should expect to see continued support for economic reform and democratization.

E. SUMMARY OF JAPAN'S ECONOMIC INVOLVEMENT IN LATIN AMERICA'S DEVELOPMENTAL PHASES:

The influence of Japan on Latin American economics becomes significant as it progresses through the developmental phases presented in this chapter.

In the first phase (1952-1976) Japan rose above the ashes like a Phoenix, emerging as an economic entity establishing global "mini" market enclaves. While Japanese participation in the region grew under the watchful eye of Washington, Japan's loan programs and import substitution industries were instrumental in Latin America's economic growth.

In phase two (1976-1988) Japan awakened to the economic and political dynamics in Latin America taking a strong stance

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[19] "Finance: Falling in Love Again," <u>The Economist</u>, 22 August 1992.

against U.S. policy. The Japanese government established its own plan to assist in debt resolution as well as supporting the plan presented in agreement with the U.S. and the International Monetary Fund. Japan emerged as an independent decision maker and ruthless financial manager.

In phase three (1989-Present) there has been a partnership between the United States and the Japanese cooperation to support democratic governments and economic reforms. Also there will continue to be a strong focus on economic growth in the region with a strong Japanese presence with which the United States will have to come to terms.

These three phases of economic developmental growth and the significance of Japanese influence in Latin America set the stage for further discussions concerning specific economic relationships in the region. The next chapter will address the emergence of global economic trading regions and the role of Latin America.

III. BUILDING BLOCS

In one form or another Free Trade Areas (FTA) have been in existence since World War II. In this chapter the foundations of building FTA's, also known as Economic Blocs, are explored with a focus on the implications for the Latin American region.

A. HOW ECONOMIC BLOCS ARE BUILT

The formal General Agreement on Tariffs and Trade (GATT) negotiations began in Geneva in 1947. These and subsequent discussions have focused primarily on tariff reduction issues. Each round of talks took longer to reach any agreements and member nations became disenchanted with the lack of conclusion. By 1963, concerns over growing protectionism were added to the agenda. The Tokyo Round, held in the mid-1970's also addressed the continuing protectionist trends but failed to resolve any safeguards agreement.[20] The Uruguay Round, started in 1986, remained deadlocked in October 1992.[21] Although the GATT issues have finally been resolved at the December, 1993 meeting in Geneva, the past stalemate of

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[20]Enzo Grilli, "Macro-Economic Determinants of Trade Protection," World Economy, September 1988, p. 322.

[21]Sylvia Ostry, "The Uruguay Round: An Unfinished Symphony," Finance and Development, June 1991, p. 16.

discussion and perceived lack of direction had encouraged countries to continue and even enhance their regional economic affiliations.

Regional economic affiliations can lead to the formation of free trade areas (FTA) or sometimes referred to as Economic Trading Blocs. FTA's eliminate barriers to trade at the border between partner countries by means of a formal treaty while preserving the right to independent action in external relations. The FTA creates a preferential access to each others markets, thusly creating an economic "bloc."

The European Community (EC) is undeniably the oldest free trade area in existence today. The EC foundation was in the Marshall Plan that aided in the reconstruction of Europe after World War II.[22] This support encouraged Europeans to relax trade restrictions and by 1950 formal trade specific cooperative talks were held. By 1970, member states had removed tariffs and created the infrastructure inherent to a free trade area as we know it today. The EC structure speaks for itself in its effectiveness. European Community trade grew twice as fast as the rest of the international economy.[23] The further steps taken by the EC, under initiatives from Germany in the late 1980's, have been

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[22]Herbert E. Weiner, "America's Role in the Founding of the European Community," The Growth of Regional Trading Blocs in the Global Economy, (National Planning Association, 1990), p. 57.

[23]John Pinder, The European Community: The Building of a Union, (Oxford University Press, 1991), p. 61.

construed by some as the development of a hostile economic regional trading bloc with a goal of complete economic integration.

The United States and Canada have had a free trade agreement that began with the Reciprocity Treaty of 1874.[24] A relatively close relationship has continued since, highlighted by free trade agreements in agricultural equipment in 1944 and automotive products in 1965.[25] The integration over the years has evolved into an increasing level of comfortable interdependency. In 1992, 74% of Canada's total trade was the U.S.; 78% of Canada's 1992 exports were to the U.S. and 71% of its imports were from the U.S.[26] To include Mexico in a North American Free Trade Area (NAFTA) would result in a market that would rival that of the EC with a combined 1990 gross domestic product (GDP) for North America at $5.9 trillion compared to $4.4 trillion for the EC.[27]

The intention of NAFTA negotiations has been to make the agreement profitable to all three countries. The liberalized

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[24]Maureen A. Farrow and Robert C. York, "Regional Trade and Trends: A North American View from the Inside Out," The Growth of Regional Trading Blocs in the Global Economy, (The National Planning Association, 1990), p.83.

[25]Gary Clyde Hufbauer and Jeffrey J. Schott, North American Free Trade : Issues and Recommendations, (Washington, D.C. Institute for International Economics, 1992), p.3.

[26]"How To Make It in The World Market," Trade and Culture, v. 1, n. 3, Fall 1993, p. 95.

[27]World Development Report 1991 (World Bank 1991)

trade relationships will eliminate customs duties on "tens of thousands of items" over a 15 year period. [28] In addition to this continental free-trade zone there is the potential of eventually including the rest of Latin America in an "Americas Free Trade Area." Because of the growing economic interdependency and geographical contiguity, the Americas trading relationships would result in growing regional linkages. A regional "Americas" trading area is the most likely result as expressed by President Clinton.

The Asian Free Trade Area (AFTA) is being nurtured by the Association of Southeast Asian Nations (ASEAN), which was created in 1967. The ASEAN was intended to accelerate economic growth, social progress and cultural development in the region. [29] Under Japan's impetus since 1987, the dormant association has come to life. During the January 1992 Singapore summit, the commitment to ASEAN economic cooperation gained momentum. Arguably, this summit may have been in response to European and North American free trade area initiatives. At this meeting, member nations decided to

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[28]Keith Bradsher, "Headway on North American Trade Talks," <u>The New York Times</u>, 3 August 1992, p. C1.

[29]Lawrence B. Krause, "The Bangkok Declaration of ASEAN," <u>US Economic Policy Toward the Association of Southeast Asian Nations</u>, (The Brookings Institute, 1982), p. 6.

accelerate joint efforts in enhancing intra-ASEAN cooperation and establishing an ASEAN free trade area. [30]

Another factor promoting Asian economic regionalism has been the U. S. negotiation of free trade areas in the Americas, because it signaled the failure of America to provide support for global free trade under GATT.[31] Regardless of the recent resolution of GATT differences, regionalism is a formidable economic issue.

When the Asian free trade area is completed it would have a combined GDP to rival that of the EC or NAFTA (Table 3-1) giving it a greater voice in international trading relations.[32] This ability to act in a unified manner on international trade issues may be a determinant in the success of the free trade areas.

B. ETHNIC INFLUENCE

Latin America became Japan's principal post-war emigration outlet. Large numbers of immigrants from Japan relocated to Latin America with over 100,000 settling in Brazil; 80,000 in Peru; 30,000 in Argentina; 10,000 in Bolivia; and smaller

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[30]"The Singapore Declaration of 1992," ASEAN Economic Bulletin, v. 8, n. 3, p. 376.

[31]Stephen W. Bosworth, "The United States and Asia," Foreign Affairs, Spring 1992, p. 122.

[32]Augusto de las Torre and Margaret R. Kelly, Regional Trade Agreements, International Monetary Fund Occasional Paper 93, March 1992, p. 4.

TABLE 3-1

FREE TRADE AREAS	1990 GDP
EC	$4.4 trillion
NAFTA	$5.9 trillion
ASEAN	$3.5 trillion

Source: International Monetary Fund (1992)

numbers in Paraguay and Uruguay.[33] The government of Japan understood the economic importance of these ethnic Japanese enclaves, as well as the limitations of their island nation. The economic importance of establishing an import source for raw materials and food was paramount. Japan looked toward Latin America, using the Japanese communities in these various countries to aid in market establishment and to facilitate the trading relationships.

Trade relations between Japan and Latin America, virtually non-existent in the 1950's, increased from $600,000 in 1960 to 15 billion by early 1980's.[34] Japanese communities assisted in establishing trading relationships between their new countries and the motherland. Internal markets were made available, as well as minerals and other raw material resources. Japan must import virtually all its raw materials and food supplies; whereas, the Latin American countries needed to export them: it made for a marriage of convenience.

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[33]Atkins, p. 104.

[34]Atkins, p. 104.

However, more recently the second and third generations of these original Japanese immigrants resent being used by Japan since they now consider themselves as Brazilian, Peruvian, etc. first and of Japanese heritage second.

The relative importance of these Japanese ethnic enclaves on trade can be determined from Table 3-2.[35]

TABLE 3-2
LEADING LATIN AMERICAN COUNTRIES IN JAPAN'S TRADE WITH THE REGION

1991

Imports from Japan	% share of region	Exports to Japan	% share of region
Mexico	22.0	Brazil	32.3
Brazil	9.6	Chile	19.2
Chile	4.9	Mexico	17.7
Argentina	3.5	Argentina	6.1
Paraguay	1.1	Peru	4.0

Source: A. Blake Friscia "Japanese Economic Relations with Latin America," Japan and Latin America in the New Global Order, 1992

The case of ethnic dependency as a factor in Japan's trading policies or economic strategy can not be justified by the weight of the various total exports to and imports from, the region. The share of trade between Brazil and Japan is predicated on the sheer size of Brazil and its perceived unlimited raw materials needed by Japan. The table indicates Mexico and Chile as significant trade partners but neither has had the advantage of any Japanese ethnic communities to work as a catalyst. Admittedly it is difficult to extrapolate the

[35] Friscia, p. 16.

impact of ethnic dependency without specific data on known market cases. However, presented here in the simplest form the available data does suggest the invalidity of hypothesis #1: that Japan's interest in Latin America is generated by the post World War II Japanese immigration to the region.

C. DOLLARS AND SENSE

The early allure of Latin America for Japan was the unlimited raw materials and resources of the region. As early as the 1950's, heavy investments were put into mining, agriculture and oil exploration in Mexico. The oil shocks of the 1980's and the exclusion from the Alaskan oil source forced Japan to become the second largest oil customer of Mexico's PEMEX (oil).[36] Japanese firms were willing to invest in joint ventures with the Mexican government as a minority partner, as in the case of NKS (steel) and PMT (oil related equipment).[37]

Although relations were strained at times over debt, mismanagement and corruption in industry, Mexico held the trump card in its vast oil reserves. To secure the oil source, in 1980 the Japanese entered into a long term

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[36]Luis Rubio, "Japan in Mexico: A Changing Pattern," Japan and Latin America in the New Global Order, (Lynne Rienner Publishers, 1992), p. 71.

[37]Rubio, p. 72.

agreement for 100,000 barrels of PEMEX oil per day for a ten year renewable contract.[38]

In the last decade the Japanese have continued to take advantage of cheap labor in Mexico and have expanded investments from the maquiladoras plants where activities have tripled from 1987 to 1989. Under the "maquiladora" program, U.S. or foreign firms that are located in the United States can ship U.S. made components to Mexico, assemble them in Mexico at the maquiladora plants, and then have them shipped back to the United States under favorable tariff conditions. Since the maquiladoras are in reality export processing zones, they do little to enhance the competitiveness or economic growth for Mexico other than basic salaries and minimal infrastructure. Virtually all Japanese exports from Mexico are directed at United States markets and only 14% of profits stay in Mexico.[39]

Brazil's natural resources also attracted Japanese trading companies in the early 1950's. Products from lumber, mining and agriculture were the initial investments. However, by 1980 major investments had been made in thermal power plants;

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[38]Miguel S. Wionczek and Miyohei Shinohara, "Las Relaciones Economicas entre Mexico y Japon: Influencia del desarrollo petrolero Mexicano," (Mexico: El Colegio de Mexico, 1982), p. 71.

[39]Rubio, p. 83.

petroleum exploration; port modernization and ship building; agricultural projects; and lumber mills.[40]

In foreign trade, conflict between the United States and Japan has generated a degree of cooperation between Japan and Brazil. When President Nixon announced the soybean embargo in 1973, Brazil and Japan entered into an agricultural joint venture to solve the supply problem. The results were that soybeans have displaced coffee as Brazil's leading cash crop.[41] Under Japanese influence, by 1984, Brazil had the entire Asian soybean market.

The promotion of cheaper beans from Brazil reduced the cost of Japan's agricultural imports. Enter the consummate trader- the more beans on the market, the lower the cost. This is a simple supply and demand pricing issue in Japan's favor. Other products Japan depends on Brazil to supply include: coffee beans, iron ore, tobacco, beef, cocoa butter, sugar, orange juice, fuel oil, steel products and organic chemical products.[42]

Although Brazil and Japan continue to have problems due to the debt crisis resolution, cultural differences and

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[40]Riordan Roett, "Brazil and Japan: Potential versus Reality," Japan and Latin America in the New Global Order, (Lynne Rienner Publishers, 1992), p. 48.

[41]Leon Hollerman, Japan's Economic Strategy for Brazil, (Lexington Books, 1988), p. 226.

[42]CACEX, (Foreign Trade Dept, Central Bank of Brazil, 1988).

nationalism, there still remains an economic dependency. Japan desperately needs to import the raw materials and food resources while Brazil needs to export them to try to salvage its economy.

Japan's economic strategy in the region has been impressive. Japan has an "unlimited" supply of natural resources, raw materials and food at the lowest possible import price. These strategies have helped Japan become the economic dynamo that it is today. Basic economic theory, perfected by the Japanese, supports that imports at the lowest cost with exports at the highest cost, yields a substantial trade surplus.[43]

D. PROSPECTS WITH THE PACIFIC

Although the basic demands of economics are most certainly a driving force for Japan's activities in the Latin American region, the drive toward a Pacific Rim trading area is prevalent as well. With the emergence of the economic "Triad" i.e. the free trade areas of the EC, NAFTA and ASEAN, there is a real concern of trading bloc "lock-out."

Japan has used its economic influence in Mexico to gain access to American markets under various guises. Currently, the maquiladora assembly industries represent 34% of Japanese firms in Mexico, with Nissan being the largest with 55% of all

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[43]Franklin R. Root, International Trade and Investment, (South-Western Publishing, 1990)

Japanese investments in Mexico.[44] Mexico's appeal to Japan has been the potential NAFTA market source. Japanese firms are currently expanding maquiladora facilities to take advantage of the new trade policies. In other words, Japan is trying to get its foot in the door of NAFTA.

Another approach is that Japan wants Mexico to propose to the United States a joint Mexican-Asian Pacific maquiladora arrangement.[45] Additionally, Japan is trying every avenue possible to entice Mexico into an trans-Pacific trade agreement. This includes Japan's lobbying of the East Asian Economic Council (EAEC) from excluding Pacific Basin countries. This is all being done as a preventive measure from a North American trading bloc exclusion of Asian countries.[46] Countries other than Mexico that front the Pacific have also been targeted for Japanese economic maneuvers to gain access to Latin American and United States markets.

Since 1991 Japan has become Chile's largest export market. The natural resources of minerals, lumber, fish and agriculture are necessary for Japan's economy. Japan has

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[44]Friscia, p. 25.

[45]Riordan Roett, Mexico's External Relations in the 1990's, (Lynne Rienner Publishers, 1991), p. 151.

[46]Purcell p. 142.

invested over $700 million in Chile in the last two years. [47] Additionally, the number of Japanese-owned companies in Chile has doubled in the past two years.

Most economist are wondering how Chile penetrated the Japanese market. More importantly, Chile has provided an important foothold for Japan in Latin America. Terusuke Terada, foreign minister in charge of Latin American affairs, said in an interview in Chile's leading newspaper, El Mercurio, "...Chile has to be pushed closer to the Pacific Basin...."[48]

Chile wants to be the "bridge" of choice for the Pacific Basin countries into Latin America. Also, Japan hopes to use Chile along with Mexico, to circumvent tariff barriers in the Latin American markets and ultimately into the North American markets.[49]

President Fujimori has encouraged the Japanese investors to Peru and is actively negotiating Japanese investments in Peru's radical privatization program.[50] Given Peru's reputation as a high risk nation, properties are considered to

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[47]Nathaniel C. Nash, "Chile: Japan's Backdoor to the West," The New York Times, 15 April 1993, p. C1.

[48]Nash, p. C6.

[49]Ibid.

[50]James Brooke, "Privatization to Reshape Peru Market," The New York Times, 4 April 1993, p. C1.

be among the cheapest in the world and a good buy for the Japanese.

These economic ties and trading practices being aggressively pursued along the Pacific Latin American countries could be perceived as an attempt to outflank an Americas trading bloc "lock-out." Therefore, it is important to understand the dynamics of the world economic actors.

In the next chapter these dynamics are presented with an emphasis on the U.S.- Japanese relationship and the implications for Latin America.

IV. ECONOMIC ACTORS

This chapter will discuss the unique roles of the United States and Japan in the international trade system. The move toward more American nations becoming trade partners within the region and Japan's perceived victimization of economic bloc "lock-out" are issues addressed. Additionally the controversial Japanese trade practices in Southeast Asia are examined with a look at the paradigm's application in Latin America.

A. THE MAIN PLAYERS

Over the past several years, the international trade system has been challenged. Currently, the world trade system is characterized by regional interests. This is a result of the separate but interrelated decisions of the main players who together shape the international economy- the governments of the "Triad" of the United States, Japan and the European Community.[51]

As early as 1984, the Japanese were opposed to the United States shift in trade policy that could lead to the formation of trading blocs. The Japanese claimed that "negotiating with only like-minded countries would leave aside trade with

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[51]Sylvia Ostry, "The Implications of Developing Trends in Trade Policy," Business Economics, January 1990, pp. 23-27.

developing countries."[52] However, one could argue that bloc countries already do a disproportionate amount of their trade with one another anyway.

At the Federal Reserve's summer conference in 1991, the bankers saw 5 reasons to support trading blocs:[53]

1. The GATT had outlived its usefulness;
2. Trading blocs reduce national tariffs and trade barriers;
3. Statistics show that blocs generate substantial increases in trade among partners;
4. GATT-style free-trade, tariff-reduction solutions had failed to deal effectively with non-tariff barriers; and
5. Trading blocs can be an effective way to compete with Japan.

The United States has fostered the regional free trade idea since the 1961 inception of the Alliance for Progress (an economic plan intended to promote trade among the countries of North, Central and South America). Although the Alliance was considered a political failure, intra-regional trade did increase and the foundations were set for the continuation of that pattern.[54]

With the mechanism for NAFTA in place, the United States has been and continues to pursue trade agreements with other

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[52] "World Trade: A Risky Shift in Trade Policy," Business Week, 12 November 1984, p. 34.

[53] Joseph L. Brand, "The New World Order: Regional Trading Blocs," Vital Speeches, 15 December 1991, p. 155.

[54] Ronald Scheman, The Alliance for Progress: A Retrospective, (Praeger, 1988), p. 50.

countries in the Latin American region. Such proposals are part of the initiative for the Americas to promote intra-Americas trade. The Enterprise for the Americas was comprised of planned new partnerships for trade, investment and growth proposed to create economic links between countries in North and South America.

President Bush announced the Enterprise for the Americas Initiative in summer 1990. In the first year agreements were signed with 16 Latin American countries. By June 1991, NAFTA representatives had met with the MERCOSUR countries of Brazil, Argentina, Uruguay and Paraguay and discussed an agreement aimed to change and enhance trade relations between the two groups.[55]

By July 1991, a consortium of 13 Caribbean nations signed trade agreements. The agreement with the Caribbean Community (CARICOM) included Antigua; the Bahamas; Barbados; Belize; Dominica; Grenada; Guyana; Jamaica; Montserrat; St. Kitt and Nevis; St. Lucia; St. Vincent and the Grenadines; and Trinidad and Tobago. Remarkably, the United States has signed trade agreements with a total of 29 American nations with just Cuba, Haiti and Dominican Republic outside the trade pact.[56]

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[55] "EUA, parcevus do Mercosul," South American Business Information, 14 June 1991.

[56] "U.S.-Carib Free-trade Talks," News, 5 August 1991, p. 29.

Although the Japanese have complained that the move toward a Western Hemisphere trading bloc is an attempt to lock them out, the reality is that the Enterprise for the Americas is the federal government's response to the EC's unification plan to establish a 12-country free trade zone.[57] The results of the union are likely to be increased intra-European trade and diminished demand for U.S. products. However this may change with the recent GATT agreement resolution.

Noted economist, Jagdish Bhagwati, recently wrote that the Clinton administration indulges to excess the misperception of U.S. declinism.[58] There is a view that America has disarmed itself unilaterally in trade while others compete in "unfair" trade practices. Could it be true that the main motivation toward regionalism is protectionist: Mexico and Latin America become the United States preferential markets, with Japan and the EC at a disadvantage? Is that not what the EC unification intended as well? Where does this leave Japan and Southeast Asia?

Currently, Japan, projected as the economic dynamo of the 1980's is in financial trouble in the 1990's. The bubble burst early in 1990 when the stock market lost half its value

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[57]Brenda A. Jacobs, "Enterprising Initiatives Abound," Bobbin, v. 32, n. 2, October 1990, pp. 14-18.

[58]Jagdish Bhagwati, "The Diminished Giant Syndrome: How Declinism Drives Trade Policy," Foreign Affairs, Spring 1993, p. 22.

in just a few months. The 1992 collapse of inflated asset prices and the failure of businesses with debt of 5.2 trillion yen only added to the banking problems.[59] The International Monetary Fund (IMF) forecast an unusually slow growth for Japan at a mere 1.3% for 1993, the same as last year, compared to 3.2% growth for the United States.[60] Add to these problems the complaints in Japan of weak leadership and you have the symptoms of economic fracture.

According to economist Peter Drucker, "Japan, INC." is in disarray. The four basic pillars of Japanese policy have collapsed or are tottering. The assumptions are:[61]

1. Due to the cold war the U.S. would subordinate economic interests to the maintenance of Tokyo's political stability.

2. Dominate world markets by projecting Western trends, but do it better and faster.

3. Japan's domestic economy was immune to outside troubles (based on imports of raw materials and exports of manufactured goods- this equation still works).

4. There is stability in commitment to long term policies.

Already Japanese companies have shifted from the traditional strategy of outguessing and pirating from Western competitors to genuine research for innovative ideas. The main premise of Japan's foreign policy is that the country's

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[59]"Japanese Banks: From Bad to Worse," p. 99.

[60]Steven Greenhouse, "IMF Warns of Sluggish '93 Growth," The New York Times, 27 April 1993.

[61]Peter F. Drucker, "The End of Japan, INC?: An Economic Monolith Fractures," Foreign Affairs, Spring 1993, pp. 10-13.

security depends on its economic strength. One of the problems in Japan is the lack of consensus on a new economic policy. Japan fears that the emergence of regional trading blocs could lead to a shrinkage of world trade which could cause Japan significant economic hardship.[62]

Despite all Japan's rhetoric about trading bloc victimization, the Japanese continue to exploit Southeast Asia by dominating the trade in the region. The Japanese have an economic model in which Japan controls everything and they have applied it toward Southeast Asia. They began with direct foreign investments (DFI) into manufacturing which began a cycle of dependency for the region. Japan's strategy includes not just finished goods but parts and equipment upon which the Asian exports depend. The regionalism is being promoted under the auspices of ASEAN with the Japanese as the motivator. However, the southeast Asian countries are now starting to fight back.

The Japanese have begun to realize that their single-minded pursuit of affluence and the use of their wealth in an attempt to win friends and influence people in the outside world is not always successful. In 1991, the Japanese Prime Minister, Toshiki Kaifu, said that Japan was becoming

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[62]"Japanese Fearful of Regional Trading Blocs," Financial Times (London), 4 December 1991, p. 7.

politically, as well as, economically active in trading regions.[63]

This new geopolitical approach can be best exemplified in South America. After Mr. Fujimori's seizure of near dictatorial powers in April 1992, the international community isolated the President of Peru; however, the Japanese government continued to provide hundreds of millions of dollars in vital foreign aid. In Chile, the Japanese made a political move to push their favorite presidential candidate, Eduardo Frei, and had even invited him to Japan on an official visit just months prior to the election.[64]

These moves toward security for investments, trade agreements or even future economic policies in Japan's favor, such as Latin American market access and blocking a regional trade "lock-out", could be viewed as motivated by a bigger geo-strategic necessity as presented in the second hypothesis.

B. THE UNDERSTUDIES

With the onset of the Latin American debt crisis in 1982, the Japanese understandably looked elsewhere to make investments and for economic development. The logical choice was their own backyard- Southeast Asia.

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[63]"Japan: Affluence with Influence," Far Eastern Economic Review, 20 June 1991, p. 41.

[64]Nash, p. C6.

The understudies of Asia fall into two categories: 1) the newly industrialized countries (NICs) of Hong Kong, Singapore, South Korea, and Taiwan, sometimes referred to as Asia's Dragons; and 2) the "new NICs" of Indonesia, Malaysia, the Philippines and Thailand, sometimes referred to as Asia's New Little Dragons.

The Japanese paradigm of economic development utilized in Southeast Asia describes a phenomenon in which a group of economies, closely interacting with one another, advance together as a whole, led by a predominant economy as the growth center, followed by progressively less developed economies in a hierarchical pattern.[65] The internal sequencing is a matter of gradual development as evidenced by the emergence of Asia's Dragons and new Little Dragons.

The Japanese have applied a little noticed policy to promote greater integration of the region by using a mix of Japanese government and private resources. In this way, Japan feels that it can nudge the political leadership in the direction it wants by virtue of the dint of its money.[66] However, in 1989, both the president of Singapore, Mr. Lee Kuan Yew, and Dr. Mathathir Mohamad, prime minister of Malaysia, made political statements about strong American

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[65]Terutomo Ozawa, "The Dynamics of Pacific Rim Industrialization," Mexico's External Relations in the 1990's, (Lynne Rienner Publishers, 1991), p. 131.

[66]Paul Maidment, "The Yen Block: A New Balance in Asia?," The Economist, 15 July 1989, p. 5.

presence for regional security. Both men touched upon a nagging distrust of a more assertive Japan.[67]

Other Asian countries are also setting their priorities. Many want the Japanese aid but not the strings attached. The anger at Tokyo trade practices is growing in Asia where they call Tokyo export policies predatory. For years the aid to East Asia has been as goods and services from Japan. Since the requirement is for Japanese manufacturing technology, a dependency cycle was established. What really angers the Asian manufacturers is that Japan will not sell its most advanced technology (its not part of the paradigm).[68] The Asians can only conclude that Japan is afraid that their products would take over Japanese markets.

At the 1991, ASEAN conference, it was considered whether East Asia should create its own East Asian Economic Grouping as an economic consultive forum. Japan's economic dependence is so great on the region that it would be compelled to cooperate.[69] With the challenge to Japanese clout in Southeast Asia, it is only a natural progression for Japan to put more emphasis on activities in Latin America to insure its economic security. Japan's economic interest in Mexico, Chile

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[67]Maidment, p. 6.

[68]James Sterngold, "Anger at Tokyo Grows in Asia," The New York Times, 13 April 1993, p. D2.

[69]"Trade: An Insurance Policy," Far Eastern Economic Review, 25 July 1991, pp. 52-56.

and Peru as Pacific Rim countries has already been discussed in regard to investments and financial manipulation. What is of interest here is the Latin American governments' determination to free their continent's trade, whether or not worldwide trade is made freer (Figure 4-1).

The MERCOSUR group and the members of the Andean Pact have taken measures toward internal free trade. The Central American Common Market (CACM) with Panama have negotiated trade with Mexico, Venezuela and Chile.[70] The Acting Finance Minister of Chile, Jorge Rodriguez Grossi, made statements in March, 1993, about the Free Trade Treaty with the United States and resumed negotiations over free trade with Colombia.[71] Chile continues its drive for free trade integration agreements with Mexico and Argentina; additionally, Chile has finalized a free trade agreement with Venezuela. Chile has been very aggressive about continental free trade, and in April, 1993, signed a trade agreement with Bolivia. This is truly a significant step since there has been no diplomatic relations between the two countries since 1962.[72] Chile has seriously reiterated its commitment to further integration not only in Latin America but with the

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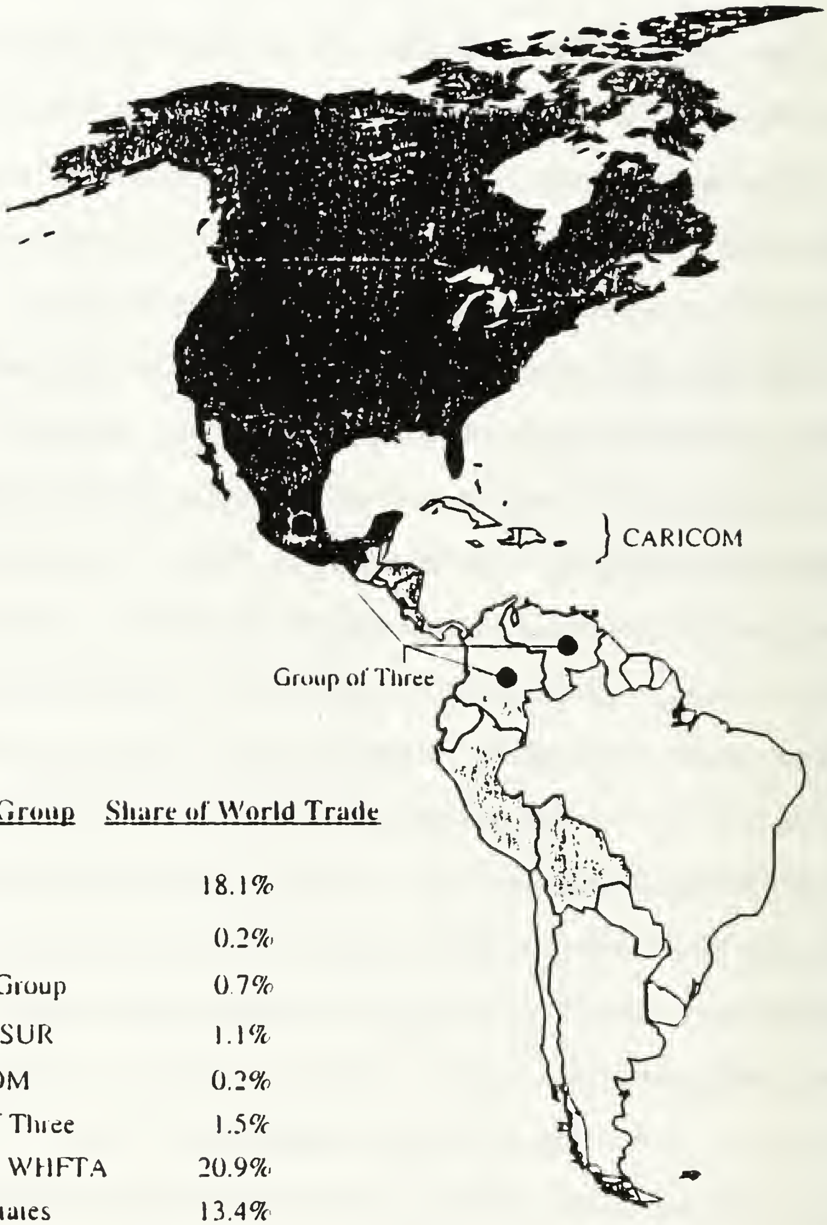
[70]"The Business of the American Hemisphere," The Economist, 24 August 1991, pp. 37-38.

[71]"Acting Finance Minister on Free Trade Treaty," Santiago HOY, Santiago, 17 March 1993.

[72]Latin American Weekly Report, 29 April 1993, p. 183.



Country or Group	Share of World Trade
NAFTA	18.1%
CACM	0.2%
Andean Group	0.7%
MERCOSUR	1.1%
CARICOM	0.2%
Group of Three	1.5%
Potential WHFTA	20.9%
United States	13.4%
Japan	7.7%
EEC	41.0%

FIGURE 4-1

Integration in the Americas and Shares of World Trade
Source: Convergence and Community: The Americas in 1993, A Report of the Inter-American Dialogue

United States, Canada and Pacific Rim countries as well.[73]

Sometimes trade is negotiated to prevent being left out, as recently reported: "CARICOM and Central American Economic Integration Treaty (CIECA) seeking to develop a common strategy to increase trade between the two sub-regions to improve negotiating power when dealing with other economic blocks."[74] This same phenomenon could explain part of Japan's economic behavior in Latin America as suggested earlier in the third hypothesis.

Mexico has led the way in the new emphasis on international trade. In a paper given by Under-secretary Minister of Foreign Affairs for Mexico, Andres Rozental, in January, 1990, he clearly lays out the economic priorities for Mexico:[75]

1. Economic cooperation in the Pacific;
2. Not to limit international economic relations to a single economic area alone;
3. Diversify Mexico's international economic policies;
4. Continue transition from highly protected economy to most open model;
5. Diversification of economic exchange does not mean its withdrawal from the U.S. market;

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[73]"Silva Cimma Remarks on Free Trade Agreements," Santiago Radio Cooperativa Network, 17 March 1993.

[74]Latin American Regional Report: Caribbean and Central America Report, 1 April 1993, p. 1.

[75]Andres Rozental, "Mexico and the Pacific: A Great Economic Challenge," given as a paper, Mexico City, January 1990.

6. The idea is to strengthen presence in new markets, while the objective is not to loose existing ones; and
7. Cooperation with the Pacific region is not to harm the Latin American sub-regional integration efforts.

Mexico's economic reforms have caught the attention of potential economic partners around the Pacific Basin.[76] Perhaps even investments for the new wealth of the Asian Dragons.

Although Mexico was praised by GATT in April, 1993 for its trade practices being among the most open in the world,[77] one has to consider the significance of the May, 1993 investment grade rated non-peso bond being issued in yen-denominated notes.[78] It is apparent that Japan continues to use its financial clout to influence internal financial and economic decision-making and policy-setting in Mexico, as well as Chile and Peru.

Mexico is Latin America's leading exporter and importer with the United States as its largest market at 70% of Mexican exports and supplying 65% of imports in 1990. Strategically, an ideal application for the Japanese economic development paradigm with Mexico as the leader for Latin America. Perhaps

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[76]Lindajoy Fenley, "Promoting the Pacific Rim," Business Mexico, June 1991, p. 40.

[77]"Mexico is Praised on Trade," The New York Times, 21 April 1993.

[78]"A Mexican Non-peso Bond is Rated Investment Grade," The New York Times, 19 May 1993.

Mexico is being groomed as the "Latin Dragon" to bridge the trade for the Pacific region.

There have been many issues presented and questions raised concerning the economic activities of the "Triad" members: the United States, Japan and the European Community. Each has at one time or another opposed trading blocs while their own regional activities were catalytic to the formation of such blocs.

The question remains whether these Free Trade Areas will become true "blocs" or interact with each other to promote world trade. Japan's activities in the Latin American region have been primarily focused on the Pacific Rim countries. This could be an indicator of bigger trade plans to interrelate the FTA's of ASIA and the Americas.

The next section will explore the economic activities of Japan in specific countries of Latin America. The country studies include Mexico, Panama, Brazil and Chile.

V. COUNTRY STUDIES

A. PANAMA: EAST MEETS WEST

From the fledgling stages of Japanese shipping in the late 1950's the Panama Canal has played an important role in getting Japanese goods to European and other markets. When President Carter renegotiated the Panama Canal Treaty it had a significant impact on Japanese economic planning due to the dependency on the canal to reach world markets. The government of Japan now looked at the Latin American region and saw its strategic importance.

With the onset of the debt problem the economic approach to Latin America has been consciously and carefully pursued by Japanese decision makers and economic planners. While agreeing to assist with debt crisis resolution via the Brady Plan, the Japanese also had their own initiative of the Capital Recycling Plan. This plan was represented as a way to recycle Japanese trade surplus money back to Latin America as official assistance and loans.

By 1988 the investments in Panama rose nearly 800% on paper.[79] Less than 20% of the established funds for Latin

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[79]Friscia, p. 19.

American assistance were granted to the region and over 50% of the funds were funneled to Southeast Asia.[80]

Investments from this fund granted to Panama were in the shipping business. The Japanese data include the exports of ships and boats to Panama, but actually are sent for shipping registry purposes in that country. For example, in 1990 $3 billion in exports went to Panama for registration under flags of convenience for Japanese shipping.[81] Remove these figures from the Japanese export data and Japan would show a 1990 trade deficient instead of $428 million surplus as indicated in Table 5-1.

Statistically, Panama is the largest importer of Japanese goods at $3.3 billion in 1991 or 26% of the total.[82] However, these are mainly Japanese exports of ships and boats for flags of convenience and are not an indicator of domestic demands in Panama. It is interesting to evaluate the difference in foreign direct investment to Latin America calculated excluding Panama versus including Panama for total percentage:[83]

The conclusion from Table 5-2 is that the U.S. remains consistent in investments post-crisis, as well as pre-debt

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[80]Stallings, p. 24.

[81]Purcell, p. 12.

[82]Purcell, p. 16.

[83]Purcell, p. 22.

TABLE 5-1
Japanese Trade with Latin America (million US$)

	Total Exports	Exports to L.A.	L.A. Share %	Total Imports	Imports from L.A.	L.A. Share %	L.A. Balance
1981	152,030	10,516	6.9	143,290	6,669	4.7	3,857
1982	138,831	9,086	6.5	131,931	6,268	4.8	2,818
1983	146,927	6,391	4.3	126,393	6,462	5.1	-71
1984	170,114	8,549	5.0	136,503	7,230	5.3	1,319
1985	175,638	8,486	4.8	129,539	6,242	4.8	2,244
1986	209,151	9,494	4.5	126,408	6,194	4.9	3,300
1987	229,221	8,760	3.8	149,515	6,355	4.3	2,405
1988	269,917	9,297	3.4	187,354	8,313	4.4	984
1989	274,175	9,381	3.4	210,847	8,870	4.2	511
1990	286,948	10,279	3.6	234,797	9,851	4.2	428
1991	314,525	12,793	4.1	236,737	9,838	4.2	2,955
% Change 1981-1991	106.9	21.6		65.2	47.5		

Japanese Trade with Other Areas in 1991

	Exports	% Share	Imports	% Share
United States	91,538	29.1	53,317	22.5
Southeast Asia	96,176	30.5	58,810	24.8
European Community	59,158	18.8	31,792	13.4
Middle East-Africa	15,888	5.1	31,203	13.1
China	8,593	2.7	14,215	6.0

Source: A. Blake Friscia, :Japanese Economic Relations in Latin America," Japan and Latin America in the New Global Order, 1992

TABLE 5-2

FDI Latin America 1986-1988

	excl. Panama	incl. Panama
U.S.	19.4%	19.3%
Japan	07.4%	32.8%

Source: A. Blake Friscia, "Japanese Economic Relations with Latin America" Japan and Latin America in the New Global Order, 1992

crisis while Japan appears to manipulate the statistics by misrepresenting Panama. The IMF stepped in to monitor the investments to Panama as reported by the Japanese Capital Recycling Plan and by the end of fiscal year 1991, Japanese investments in Panama/Cayman dropped by 50% with more investments going to Mexico and Brazil.

The Panama Canal Act of 1979 established the framework to phase out United States functions at the Canal by December 31, 1999.[84] Therefore in 1982, the United States, Panama and Japan (the second largest canal user) began to study long term alternatives to the canal.[85] The concerns included the maintenance of the infrastructure, appropriate financial administration and alternate plans to handle the increasing demands on the canal's capacity. Alternatives include widening the canal and an alternate canal site. The General Consular and Ships Directorates, Secnaves, has reported that

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[84]Atkins, p. 334.

[85]"Comision Tripartita de Estudios para la Alternativa un Nuevo Canal," Panama City Newspaper, 22 February 1993.

the Panamanian Merchant Marine fleet is the largest in the world, as 56.3 million tons were registered under its flag, representing revenues of approximately $100 million a year, as of 1 November 1993.[86]

A renewed interest in Panama has been with the recent proposal for a new container complex on Telfus Island at the Atlantic entrance to the canal.[87] An additional proposal is to build a railroad parallel to the canal.[88] Both proposals are presented as a multinational project with American, Japanese and Panamanian investors. However, the Japanese have done feasibility studies in Nicaragua for an alternate canal location that would present economic hardship on Panama if constructed.

Panama has made the effort to introduce cattle products to the international market. According to Agricultural Development Minister Cesar, Panama's cattle sector goals are to export graded meat to sell on the Japanese market and to improve milk production to produce only Grades A and B milk.[89] Provided the Panamanian government remains open to the multinational investments and the IMF economic monitoring of

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[86]El Panama America, Panama City, 3 December 1993.

[87]"US-Japanese Consortium Proposes Container Complex in Panama," La Prenza, 15 May 1992.

[88]"Sea-Land Backs Plan For Panama Boxport," La Prenza, 5 August 1992.

[89]"Cattle Industry Improvinama," Panama City Newspaper, 5 April 1993.

those investments, future economic growth of Panama is certainly promising.

B. MEXICO: LATIN DRAGON OR TROJAN HORSE

On August 13, 1982 the Mexican Finance Minister announced that his country could not continue to service its debt.[90] The U.S. government with the International Monetary Fund put together a short term rescue package. Other Latin American governments followed Mexico's example citing many reasons for the default. Although there were many internal and external problems, one of the explanations was the end of the foreign loans that these countries had become dependent upon. Timing was bad. In the 1970's the industrial developed countries were hit with a recession consequently effecting loans to third world countries. Add to this the oil shocks, increasing oil pricing, a stagnated industrial base a huge unemployed labor force and you have the formula for disaster. By the time the Brady Plan was initiated twelve countries were involved in the defaults.

The International Monetary Fund played an import role in the rescheduling process for Mexico. The United States also assisted with rescheduled payments, more loan assistance and reform policy.

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[90]Stallings, p. 10.

By 1985 the high cost of debt service and decreased exports resulted in larger capital transfers to creditor countries. This caused a further decline in investments and consumption adding to the stagnation and inflation problems of the country. Brady agreements were reached with Mexico, Venezuela, Costa Rica, and Uruguay. Furthermore, the U.S. gave Mexico a 35% debt reduction as an act of good faith. Mexico took the responsibility seriously and sought other methods of debt reduction. Among the alternative plans were:[91]

1. debt-equity swaps; which did not work too well because it didn't bring new money in and it caused inflated assets

2. selling loans on the secondary market; which has picked up in the last few years and now is one of three rising value in the market

3. converting loans to bonds; which has been working very well as a means to establish stability

The International Monetary Fund figures for 1991 show Mexico with a Gross Domestic Product (GDP) growth of 4.5%, exceeded in Latin America only by Venezuela. That growth statistic reinforces that Mexico was one of four Latin American countries to be able to convert and reschedule debt, and put it behind them.

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[91]Stallings, p. 14.

The International Monetary Fund further states "if policy reform continues, our assessment for growth in Mexico is quite positive".[92] [93]

Mexico is conditioning itself for a change in policies from the protectionism borne of fear of U.S. domination.[94] Since the United States was the original provider of markets and technology for Asia; Japan wonders why Mexico has failed to use the benefits of being a U.S. neighbor.[95] Japan's advice to Mexico is to take advantage of the strengths of the U.S. and the latecomer advantage of technological borrowing.

Mexico is ambivalent as to which economic pole to connect with. Despite frequent calls for cooperation in the Latin American region the governments and economies have not been mutually supportive. Japan is trying to woo Mexico into joining the Southeast Asian development scheme. According to Ozawa, the Asian paradigm points out the importance of sequential restructuring of a latecomer economy from one phase to the next by means of compatibility with the economy's

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[92]Better Way, p. 21.

[93]Eugene Robinson, "Why Doesn't Latin America Work?," Washington Post Review, 6 January 1992, p. 11.

[94]Joseph Love, "The Origins of Dependency Analysis," Journal of Latin American Studies, v. 22, February 1990, p. 150.

[95]Terutomo Ozawa, "The Dynamics of Pacific Rim Industrialization: How Mexico Can Join the Asian Flock of Flying Geese," Mexico's External Relations in the 1990's, (Lynne Rienner Publishers, 1991), p. 129.

prevailing factors and technological endowments as outlined in Figure 5-3.[96]

This Asian economic development pattern can be equated to what I call the "big sister syndrome"; whereby, when one daughter outgrows a garment it is passed on to the next in line who in turn when outgrown will pass it on again, etc. The Japanese see key aspects to this natural order of industrial sequencing that are vital for Mexico to understand in order to do business with Japan.[97] These key aspects include knowing what phase of industrial restructuring each rank represents, what ways each are developing new comparative advantage, and what policies are need to make the group expand and prosper. As illustrated in Figure 5-4, Japan's postwar period of economic transformation has been systematic. Japan has offered Mexico a similar plan of four sequential phases to economic development:

1. export-oriented, labor intensive, light industry
2. export-oriented, heavy industrial and chemicals
3. export-oriented, assembly based
4. research and development, home market oriented

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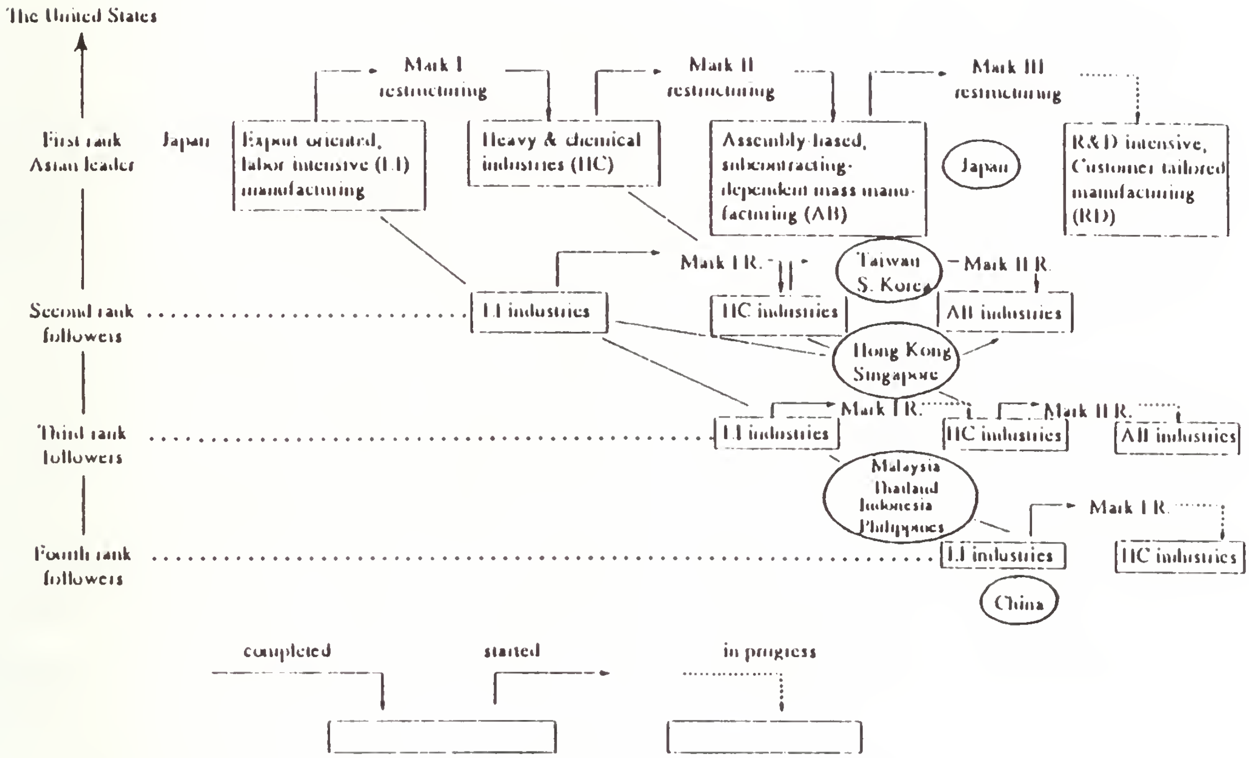
[96]Ozawa, p. 134.

[97]Ozawa, p. 143.

FIGURE 5-3

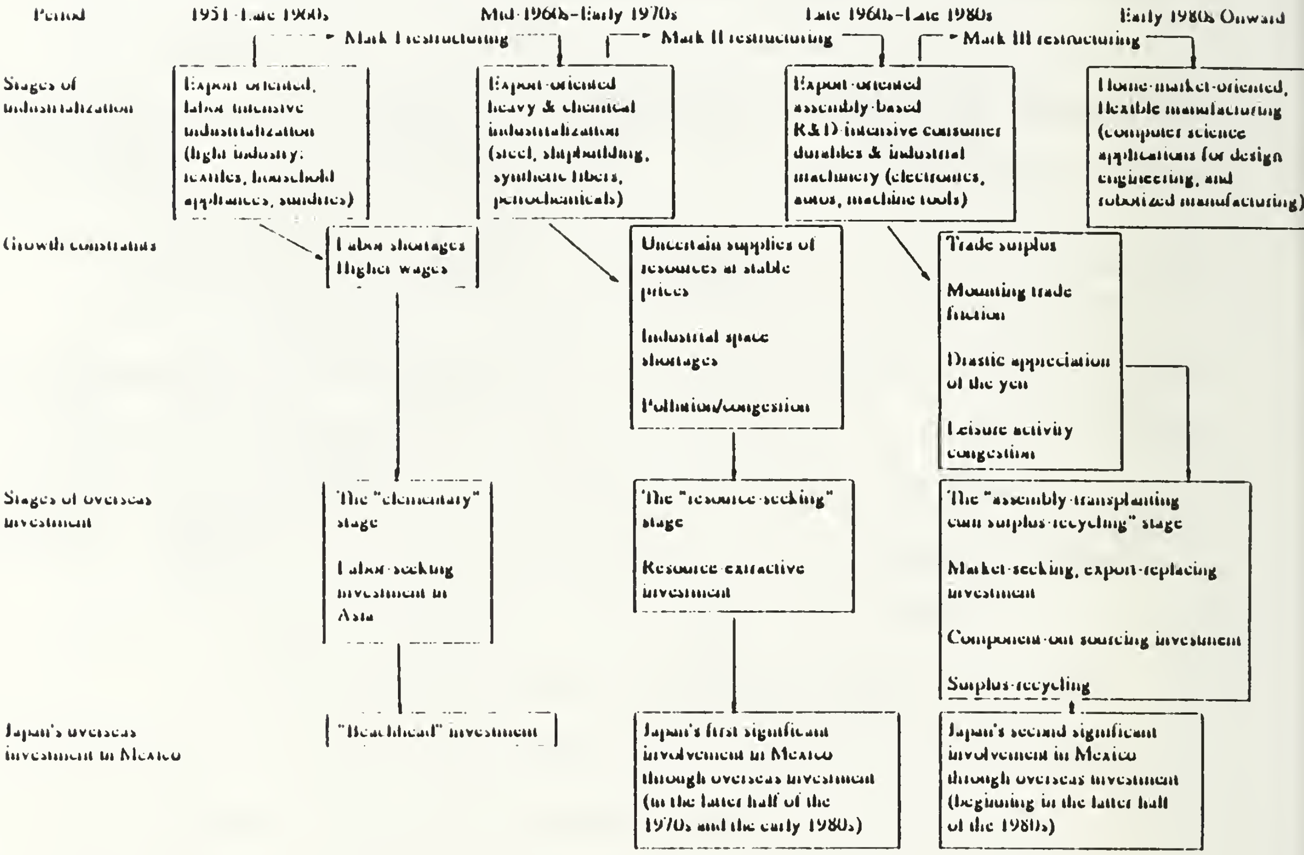
The Asian Pacific Flying-Geese (FG) Formation



Source: Terutomo Ozawa, "The Dynamics of Pacific Rim Industrialization," Mexico's External Relations in the 1990s, 1991

FIGURE 5-4

Japan's Postwar Economic Transformation: Industrialization, Constraints, Overseas Investment, and Investment in Mexico



Source: Terutomo Ozawa, "The Dynamics of Pacific Rim Industrialization," Mexico's External Relations in the 1990s, 1991

The emphasis is on the importance of industrial linkage which is the transfer of equipment, technology, etc. to the next level i.e. a systematic industrial transplant.[98]

Japan is offering Mexico a position in the ranks, so to speak; however, it would be in a Phase 1 level behind the four Asian junior tigers. This raises the issue of Japan's motive given that Mexico is doing so well and is considered a Newly Industrialized Country (NIC) versus the junior tigers who until very recently were categorized as Late Developing Countries (LDC). Could it be that Japan is looking for some place for the four juniors: Hong Kong, Singapore, South Korea and Taiwan to invest? Could it be that Japan is looking for more profits from the "maquiladora" to go back to Asia? Since with this assembly industry type of investment there is an expectation of recouping investment plus profit it is not a surprise that repatriated investment income would far outstrip reinvested income to the facility.

The driving force behind direct foreign investment (DFI) is access to either raw materials or low cost inputs (i.e. labor). Currently, the maquiladora assembly industries represent 34% of Japanese firms in Mexico, with Nissan being the largest with 55% of all Japanese investments in Mexico.[99] As Paus points out, the role of DFI in the development of

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[98]Ozawa, p. 141.

[99]Purcell, p. 25.

Latin America depends on whether and how the needs of Latin American countries coincides with the needs of the multinational corporation.[100] Mexico's appeal to Japan has been the potential North America Free Trade Zone.

Japanese firms are currently expanding maquiladora facilities to take advantage of the new trade policies. With the industrial expansion there is an anticipated population move to the economic development area.[101] This expansion of industry and labor will require additional facilities to be built further south resulting in an uneven economic growth pattern in Mexico. Additionally, since the maquiladoras are in reality export processing zones, they do little to enhance the export ability and competitiveness of the host country.[102] Although Salinas openly supports the Japanese influence in Mexico, Ocampo says that the level of influence harms national sovereignty, a fact which would become a major source of irritation to the people.[103]

Along with the maquiladora facilities, the continued interest in raw materials and oil, Japan is also looking at

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[100]Paus, p. 222.

[101]Gershon Alperovich, "Economic Development and Population Concentration," Journal of Economic Development, v. 41, October 1992, p. 64.

[102]Paus, p. 237.

[103]Jose Antonio Ocampo, "New Economic Thinking in Latin America," Journal of Latin American Studies, v. 22, February 1990, p. 178.

Mexico as a leader in a new trading scheme. Japan is looking at nations fronting the Pacific Ocean to add a Trans-Pacific dimension to trade. For example, President Salinas and the governor of Guadalajara, Carlos Rivera, are currently negotiating with Japan on a 1000 acre industrial park joint venture in Guadalajara. The site represents $70 million future investments from Asia.[104] Japan has also been actively lobbying the East Asian Economic Council (EAEC) from excluding Pacific basin countries. This is being done as a preventative measure from a North American trading bloc excluding the Asian countries.[105]

The government of Japan is enticing the government of Mexico into undertaking the initiation of several innovative measures to the United States. One is for the government of Mexico to propose an economic cooperative program to be administered jointly by the United States and Japan. The second is Japan wants Mexico to initiate a proposal for a Mexican-Asian Pacific maquiladora program in exchange for the expanded use of the present Mexico-United States maquiladora arrangement.[106] Japan claims this would neutralize U.S. criticism of Mexico's maquiladora as a Trojan Horse to hide exports from Asia. If the maquiladora continues to be used

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[104] "Construiran un Parque Industrial con Recursos Japoneses y Jaliscienses," IMPACTO, n. 2290 e Nero 20 de 1994.

[105] Purcell, p. 142.

[106] Ozawa, p. 151.

one-sidedly by the Asian economies, there is a danger that the U.S./Japanese relationship will become even more strained.

However, foreign investments in Mexico exceeded $1 billion in April, 1993.[107] If foreign investments and trade patterns continue with a Pacific focus, then Mexico could develop into a Latin Dragon.

C. BRAZIL: SEARCH FOR STABILITY

The original lure of Japan to Brazil was the internal market and natural resource base. As a Japanese publication put it:

> The appeal of Brazil is different from that of other newly developed countries, and lies in its extensive and fertile landscape, its abundant underground resources, and its diverse make-up of racial and ethnic groups. The source of Brazil's vitality lies in its diversity and creativity.[108]

So it can be said that foreign investment appeal depends not only on the economic conditions in Latin America but also by the relative attractiveness of the region versus others as a profitable investment.

As stated earlier in this paper there has been a large Japanese-Brazilian population since World War II. Initially these groups assisted with establishing markets during the early stages of economic penetration. However, more recently

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[107] "Evolucion de la inversion extranjera en Mexico duran Abril de 1993," Nacional Financiera, Mexico City, 1 July 1993.

[108] Roett, p. 101.

these people resent being used by Japan since they now think of themselves as Brazilians first.

The mid 1950's saw an import substitution industrialization encouraging Japanese investments. Additional investments included the 1958 USIMINAS steel venture and the 1959 ISHIBRAS shipbuilding venture. By 1961 Japan had $158 million invested in Brazil.[109]

By the mid 1960's Brazil had opted for economic growth rather than fiscal entrenchment and now became the perfect candidate for the Japanese "loan pushing".

The 1970's saw a stagnation in the import substitution industries as explained by Joseph Love, "the ISI had failed because of lack of dynamism of the export sector, coupled with the fact that ISI had not diminished capital and fuel import requirements."[110]

Other problems included ceilings on domestic markets, highly skewed income distribution and lack of skilled labor. The skewed income distribution is also cited by the United Nations Development Programme as a founding factor in Brazil's socialization problems.[111] The "Brazilianization" added to the economic woes. The government passed laws that required that Japanese firms must use approximately 50% of domestically

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[109]Roett, p. 105.

[110]Love, p. 150.

[111]"Why the Poor Don't Catch Up," The Economist, 25 April 1992.

produced components in any manufacturing or assembly done in Brazil.[112] Insisting on high local content is self defeating since the resulting product can not compete on the world market.

With the change that occurred in the late 1970's with excelerated lending, the Japanese banks went around "official" Japan and started lending money directly to Latin American governments at their own risk. Additional investing included paper pulp, ALUNORTE aluminum refining, and CERRADO agricultural developing.[113]

With the onset of the debt crisis the Japanese banks were most vulnerable due to the non-government protected lending practices. All private bank lending came to an immediate end with the debt crisis of 1982. The outstanding debt continues to be a source of irritation between Japan and Brazil. Brazil is one of four countries not resolving the debt crisis (others are Argentina, Peru and Ecuador).

Brazil rejecting restructuring and being in the arrears in debt servicing called a moratorium on debt payments in 1987. During the mid-late 1980's official Japanese funds via the Overseas Economic Cooperation Fund had financed the following projects:[114]

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[112]Hollerman, p. 134.

[113]Roett, p. 105.

[114]Roett, p. 112.

- Paulinas thermal power plant
- Campos basin petroleum exploration
- Santos port modernization and shipbuilding
- Minas Gerais irrigation project
- Goias rural electrification project

In 1989 the government of Brazil called a second moratorium on debt payments. Japan had been trying to sell Brazilian debt on the secondary market; however, with the announced moratorium transactions were cancelled. The Japanese irritation level was now growing exponentially.

By 1990 the relations between Japan and Brazil were fragile-- the Japanese cited the unwillingness to settle the interest arrears, the pugnacious attitude toward foreign investors and the snubbing of diplomatic protocol as a few of the problem areas.

The Japanese had been "burned" by years of uncertainty in Brazil. This includes the inconsistency of the governments dealings with foreign investors ; whereas, the government would offer subsidies to Japanese firms to establish subsidiaries to produce goods necessary for the economy and once the firms were established, the subsidies were cut.[115] With the failure of Brazil to sign a restructuring agreement with the International Monetary Fund and the $8 billion in

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[115]Hollerman, p. 133.

interest arrears, Japan with the United States agreement in 1991 froze Brazil's access to any assistance funds.

The markets in Japan for Brazilian goods are decreasing and trade between the two countries was not significant in 1988 with Brazil exports to Japan at 6.7% and imports from Japan at 6.6%[116] The market continues to shrink as indicated by Table 5-5. Although Japan still needs the natural resources, there has been neither new investments nor disinvestments. The IMF figures put Brazil at stagnant Gross Domestic Product (GDP) growth for 1991 and 1992 stating that "...due to poorer than expected performance by Brazil...."[117] IMF figures showed Brazil debt service as 55% of GDP with the U.S. and Japan holding 76.1% of total loans to Brazil. Brazil's most conspicuous problem is inflation; currently running at about 30% a month. Brazilian wages paid monthly in arrears have lost 30% of their value; a bill paid six months late will have lost 90%.[118]The inflation impoverishes the poor and discourages investors.

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[116]Purcell, p. 107.

[117]Better Way, p. 21.

[118]"Onwards and Downwards in Brazil," The Economist, 13 November 1993.

TABLE 5-5
BRAZIL BILATERAL TRADE (million U.S. $)

Exports to Japan

	1988	1989	1990	% change (1989–90)
Manufactures	604.1	561.5	470.5	–16.2
Raw materials	1,831.9	1,925.1	2,237.1	+16.2
Foodstuffs	499.9	504.3	439.9	–12.8
Fuels	5.7	1.5	2.0	+33.0
Others	8.7	6.9	23.7	+243.5
Total	2,950.3	2,999.3	3,173.2	+5.8

Imports from Japan

	1988	1989	1990	% change (1989–90)
Manufactures	941.7	1,193.5	1,193.0	–0.0
Raw materials	6.1	5.8	4.7	–19.7
Foodstuffs	4.1	5.1	2.6	–48.6
Fuels	38.6	49.4	9.2	–81.3
Others	7.6	56.3	15.6	–72.3
Total	998.1	1,310.1	1,225.1	–6.5

Source: Riordan Roett, "Brazil and Japan: Potential Versus Reality," Japan and Latin America in the New Global Order, 1992

Japan has tolerated Brazilian economic behavior just enough to ensure the raw material base Japan so desperately requires. However, Chile is fast becoming the raw materials supplier of choice.

D. CHILE: CLASSIC ECONOMICS

The Chilean economic recovery and growth consists of three periods. The first falls roughly between 1972-1982 in which policy makers failed to control the peoples tendencies to live above and beyond their means. This led to the same problems that the rest of Latin America was experiencing:

- creation of large national deficits
- skyrocketing foreign debt
- financial panic

The early trading patterns of the Latin American states were overwhelmingly dominated by their powerful North American neighbors and to some extend by the states of western Europe. Unusually enough for Latin America, Chile did almost as much trade with western Europe (England, France, Germany) as it did with the United States. As indicated in Table 5-6, in 1960 37% of exports and 46% of import trade was with the United States, while the Europeans took 38% and 24% respectively. By 1986 the United States was at 22% of Chilean exports and a leading 22% of imports. The Europeans were still the leading export market with 24% and took 17% of the import market.

Japan was only at 10% of trade in 1986.[119] At that time Chile was not considered a Asian-Pacific trader and remained strongly oriented to the American and European trade.

TABLE 5-6

Chilean Trade by Region

	1960		1986	
	exports	imports	exports	imports
USA	37%	46%	22%	22%
Europe	38%	24%	24%	17%
Japan	2%	-	10%	-

Source: compiled from Financial Times 15 April 1988

The second period of economic recovery coincided with 1982-1988 and represented some economic failures as well as successes. Chile was able to address the debt crisis problem, reschedule debt with the Brady Plan and experience declining unemployment thanks to higher copper prices. In 1985, total external debt was $20.4 billion placing Chile as the fifth largest debtor in the Latin American region after Brazil, Mexico, Argentina and Venezuela.[120] Japan was only carrying

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[119]Financial Times, 15 April 1988.

[120]Robert Devlin, Debt and Crisis in Latin America: The Supply Side of the Story, (Department of Economics, Princeton University, 1986), p. 45.

9.5% of the countries debt representing $1.4 billion while the US carried 47.3% of Chilean debt at $7 billion.[121]

The third period falls roughly from 1988 to the present. During this period monetary, fiscal, financial, labor, trade and foreign exchange policies were well planned. By March 1992 Chile was the first country in Latin America to come out of the debt restructuring phase.[122] The Chilean government had no illusions of the economic recovery that has been accredited by some to be a result of the copper price boom of 1987. By 1989 Chile had worked its external debt down to $17.8 billion from a peak of $20.7 billion in 1986. Additionally, the interest-export ratio was down from nearly 50% to under 25%; inflation kept under 20% and reduced unemployment to under 7%[123]

Much has been said of the economic recovery of Chile in the past few years; whereby, Chile has now enjoyed five years of solid economic growth. Currently the economy has all the indications of a sustainable economy moving Chile into the newly industrialized country (NIC) category along with Mexico. Both Chile and Mexico can be more properly considered Pacific

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[121]Friscia, p. 29.

[122]Roger E. Shields, "Latin America: Growing Opportunities," Business Credit, March 1992, pp. 8-9.

[123]John Williamson, Progress of Policy Reform in Latin America, (Institute for International Economics, 1990), p. 38.

Latin American NICs as they become more active in the international community.

Will the reform last? The first thing to note is that Chile is probably the best managed economy in Latin America. In 1993 Chile was ranked fifth most competitive (behind Singapore, Hong Kong, Taiwan and Malaysia) of the NICs by Switzerland's World Economic Forum.[124] Chileans boast that theirs is the most open economy in the Americas with even less tariff restrictions than the United States or Canada. The basic model is classic textbook economics to open borders and play on the strengths of the country.

Importantly, it is hard to sustain an initial growth spirt based on copper prices; however, Chile's non-copper exports have grown from nearly $3 billion in 1987 to $6.1 billion in 1992.[125]

Since 1991 Japan has surpassed the United States as Chile's major export market. US-Chile trade reached nearly $4 billion in 1992 but Chile exported $1.7 billion to Japan and only $1.4 billion to the US.[126] Chile's major exports to Japan are chemicals, minerals and forestry, fishing and

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[124] "Chile Shows the Way-Or Does It?", The Economist, 13 November 1993, p. 8.

[125] Carlos Singer, "Chilean Companies Expand Throughout Latin America," Trade and Culture, Fall 1993, p. 121.

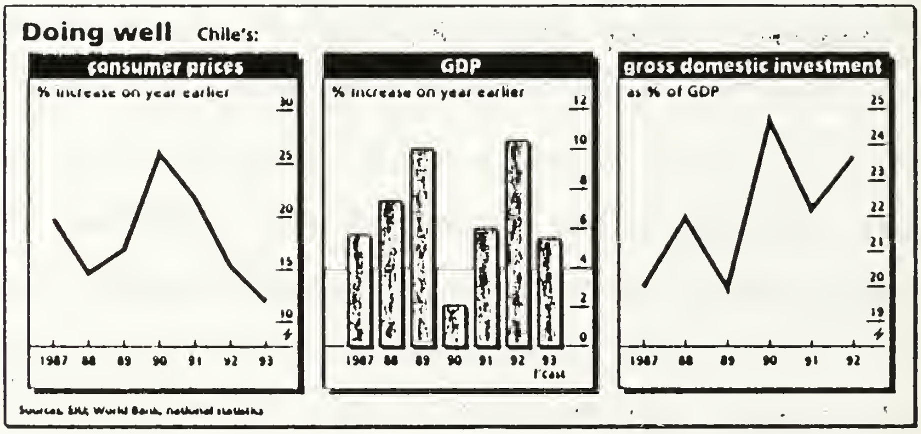
[126] Elizabeth McCarthy, "Japan is Increasing its Economic Interest in Chile," Business America, 5 April 1993, pp. 14-15.

agricultural products. Chilean imports from Japan are primarily automobiles and electronics.

The statistics tell the story (Figure 5-7). Chile's economic growth will have averaged 6% in four years, a spectacular 10.4% in 1992 giving way to 5.5% for 1993. Inflation running close to 30% in March 1990 was at 12% for 1993. Investments are running at 27% (equivalent with Asia) of GDP for 1993.[127] Most Chileans agree with President Eduardo Frei to stick with current free market policies which help keep unemployment at around 4%

FIGURE 5-7

Chile's Economic Performance



Source: The Economist, 27 November 1993

In April, 1993 Eduardo Frei, then only a presidential candidate, was invited to Japan and given presidential-style

[127] "Chile: Growth for All," The Economist, 27 November 1993 p. 52.

treatment. Shortly after the visit, Japanese companies made commitments to invest $700 million in Chile to include industrial and manufacturing joint ventures.[128] Upon winning the election, the new president reiterated his commitment to Chilean economic reform. He further stated a continued interest to seek admission to NAFTA, but also stated that Chile would join the Asian Pacific Economic Cooperation (APEC) forum in 1994.[129]

However, Chile has taken the Japanese model and adapted it to business principles to fit Chilean economic goals. Since Chile's domestic market is small, many firms realized that their long-term growth prospects were in foreign markets. Seizing the business opportunities Chilean companies are pursuing strategies similar to Japanese enterprises in Asia.[130] These strategies include:

- direct exports
- establishing a permanent presence in the target market such as Chilean managers
- establishing a bone fide company in the foreign market
- acquiring local companies
- establishing joint ventures with local companies

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[128]Nathaniel C. Nash, "A New Rush into Latin America," The New York Times, 23 April 1993.

[129]"Chile's Other Miracle," The New York Times, 14 December 1993.

[130]Singer, p. 121.

The financial wizardry continues to be impressive. The International Finance Corporation (IFC) global emerging markets indices show that from 1988 to 1992, the stock exchange in Chile rose by more than 100%, compared with a 51% increase in the United States and a 43% decline in Japan.[131]

After examining the role of Japanese firms and the shadow strategy of the Chileans, there appears a new trend first applied in import substitution, but increasingly being applied to the export sector. This new trend is called "new forms of investment" (NFI). NFIs include subcontracting, licensing, component production and franchising.[132]

Chile is untypical of Latin America in that Chile has shown how to change one of the most closed economies into one of the most open. It is doubtful that any reforms will be reversed in the foreseeable future. The people have taken ownership and private enterprise to heart and now have a vested future. The fastest growing markets for Chile are Latin America and Asia. The Chileans are doing so well on their own that even though membership has been applied for in APEC and interest remains in NAFTA, Finance Minister Alejandro Foxley stated, "the most important aspect of joining a free trade zone would be to strengthen our investment process,

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[131] "Outlook for the Stock Markets," Latin American Weekly Report, 9 September 1993, p. 416.

[132] Mikio Kuwayama, "New Forms of Investment in Trade from Latin America," Comercio Exterior, May 1993, pp. 448-497.

which is already significant today." Foxley added, "...that the signing of an agreement with North America would mean a significant boost in investors with capital from Japan, Europe, and South America, who would want to establish themselves here and use our market as a platform for entering the great North American market."[133]

Although Chile continues to supply raw materials and investment opportunities for Japan, it certainly is apparent that the Chileans have learned their lessons well in applying Japanese business strategies for the betterment of their own economy. The use of Pacific Latin American NIC markets as an entry to American markets is no longer a threat but an eventuality to be recognized.

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[133]EL MERCURIO, Santiago, 19 November 1993.

VI. SUMMARY AND CONCLUSION

A. PATTERNS AND RELATIONSHIPS

This study has shown the evolution of the significant Japanese influence on Latin American economic growth. Japan started out with a basic need for raw materials and evolved into a major economic and financial player in the Latin American region. The economic issues that were consistent throughout included the importance of raw materials; the maturation of the Japanese loan program; the diversification and implication of direct foreign investments; the struggle for independent policy decision making without causing strain with the United States; and the nurturing of the fledgling Pacific Latin American NICs.

In the country case studies of Chapter V, four very different economic relationships were analyzed with a look at the host country-Japanese economic benefits.

In the Panama study it was readily apparent that the economic relationship was asymmetrical with Japan's shipping investments for foreign flag purposes. For economic purposes Japan includes the shipping data in the total DFI for Latin America which skews the results dramatically. It is clear that the recent renewed interest in the future of the Panama

Canal to be of economic concern for Japan without political undertones.

A lengthier analysis of Mexico's economic relationship with Japan seemed appropriate given that Mexico is the closest neighbor to the United States in the region. Japanese influence played a major role with raw materials development and oil exploration. Japan played a significant role in early economic development with loans and investments. Even with the debt crisis the Mexican-Japanese relationship remained solid. Today the economic and political relationship between the two countries is on a fast track with Japan's pursuit of Mexico to become the "Latin Tiger." The direct foreign investments continue to grow with an emphasis on the maquiladora arrangements with the United States. President Salinas continues to be wooed by Japan into the Southeast Asia development network and is not resisting. Economically the relationship is still asymmetric; however, the political relationship is getting stronger as President Salinas looks for a balance against the United States. I see a "romancing" of Mexico by Japan with regional integration as the impetus and the Japanese paradigm as the method. At this time I do not see either issue as a threat to the United States. Free trade, economic growth and stability are still the United States goals as evidenced by the North American Free Trade Agreement (NAFTA).

Brazil presented a challenge in this analysis since the Japanese influence has been varied over time and the relationship between the two countries has experienced some turbulence. Raw materials lured Japan to Brazil and Japan was enchanted with the people and the beauty of the country. Significant investments in raw materials and import substitution industrialization assisted Brazil in the economic boom. With continued loans and foreign investments throughout Brazil's economic rollercoaster ride, Japan has tried to ensure the security of obtaining vital raw materials.

However, as Brazil's defiance toward debt resolution and the "Brazilianization" process increased, Japan found it difficult to justify further investments. I think that Japan will keep economically involved in Brazil just enough to ensure the raw material base Japan so desperately requires.

Not only is Chile rapidly replacing Brazil as the country of choice for raw materials but also for investment and joint venture business opportunities. Chile is atypical for Latin America in that the Chileans were able to open up the most closed economy into the most open in the region. Using the classic textbook economic approaches of free trade, the Chilean economy has recovered to the extent that Chile is considered the best investment in Latin America. Under a closely managed economy Chile has secured a place as a Pacific Latin American NIC providing viable business opportunities for Japan and other Asian investors. Interestingly enough,

Chileans have successfully adapted Japanese business models to fit Chile's economic goals. Chile has the economic interest and intent to engage both APEC and NAFTA for market resources. In addition to the natural fit of Chile into NAFTA, I see Chile becoming the "Bridge Across the Pacific" uniting markets and resources for maximum trade benefits.

Japan has shown that it approaches Latin American countries on a case-by-case basis. Each country is approached with an astute economic policy nuanced by the economic needs of Japan.

I. UNCOMMON MARKET: THE START OF SOMETHING BIG

Although a lofty prediction, it is most likely that by the turn of the century, North America, Western Europe and East Asia will be regional powerhouses of roughly equal economic strength, each with an output of $6.8-8 trillion.[134]

The question that continues to nag at economists is whether or not the Free Trade Areas are a form of discrimination and are they legal under GATT. Regionalism offers opportunity for more trade within the region, though there is possibility of some trade diversion. All this can be compatible with GATT and is even legal under GATT

[134]Melvyn Westlake, "Welcome to a Tri-polar World," Bank, v. 141, n. 735, July 1991, pp. 22-25.

regulations.[135] However, the greatest poison to the multilateral system today is neither European integration nor the prospect of a North American Trade Bloc, but rather the failure of the GATT process to open up Japan.[136] This position is supported by Robert Z. Lawrence, a senior fellow at Brookings, who states that a balance of economic power exist now between the United States and Europe; however, Japan despite its economic power, does not have this balance because of its relatively closed markets.[137]

The Pacific region will probably not become an economic force under ASEAN because Japan and the other Asian countries do not have any common affinity. In fact, most have been occupied at some point by the Japanese and have no desire for Japanese control or influence on their nations' development. However, Asian leaders do see the Pacific cooperation effort as an essential strengthening of regional trade arrangements as a step toward the globalization of free trade.[138]

Looking at the situation from a global perspective, there are two great transformations underway in world economics

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[135]Norman S. Fieleke, "One Trading World or Many: The Issue of Regional Trading Blocs," New England Economic Review, May/June 1992, pp. 5-6.

[136]Rudiger Dornbusch, "Dornbusch on Trade," The Economist, 4 May 1991, p. 67.

[137]"Trading Blocs Coming: Brookings Experts See Good, Bad," Rubber and Plastic News, 27 May 1991, p. 7.

[138]Maurice F. Strong, "Adaptations of the Blocs," Financier, April 1989, pp. 15-23.

today: 1) a transition from the American "mass production" to the Japanese perfected "lean production" (lean means using less of everything from raw materials to workers); and 2) the shift from a global international economic system to a world system composed of a few regional free trade areas.[139]

The dramatic changes in Latin American economics in the 1990's will be linked to the integration with the global economy as a cornerstone for Latin America's reforms. Japan will continue its economic development programs in targeted Pacific Rim countries for raw materials and Western Hemisphere market access; while Asia's Dragons and Little Dragons look forward to Latin American investment opportunities.

I don't perceive a strong regional yen bloc developing. As discussed in Chapter IV, Japan has problems in achieving balance between economic aggression and political diplomacy. Japan knows how to win the game; but, is short on sportsmanship. The Southeast Asian countries will not permit Japan to be the economic decision-maker for the region. The East Asian Economic Grouping will probably develop into an admirable format over Japanese economic dominance.

Although the center of global economic dynamism is shifting, a Pan-Pacific arrangement which includes the United States is most likely, probably in the APEC forum. Currently,

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[139] James P. Womack, "Americas," Latin Finance, March 1991, p. 45.

the United States and Japan dominate the Pacific Rim economically; however, China's economy is a growing force to be reckoned with in the near future. The possibility of sub-blocs within the Pan-Pacific scheme could include a yen bloc of Southeast Asia, Australia and New Zealand; a Peking bloc of China, Korea, Taiwan, Singapore and Hong Kong; the Western Pacific community of Australia, New Zealand, China, Japan, Korea, and others; and the Eastern Pacific community of Canada, the United States, Mexico, and perhaps Central and South America.[140] As you can see the overlapping trade patterns are virtually unlimited and to everyones advantage for free trade.

Future economic growth on the Pacific Rim could be effected by global economic trends, commodity prices, political problems and resistance to open markets and free trade. While creating new wealth and opportunities, free trade destroys jobs in the least competitive sectors of the economy and forces the overall system to become more efficient. The development of more efficient economies creates more jobs and increases the overall standard of living.

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[140]Kim Duk Choong, "The Pan-Pacific Card," Far Eastern Economic Review, 21 December 1989, pp. 60-61.

II. NEW REALITIES REVISITED

The regional economic blocs as presented in Chapter III are undoubtedly the way of the future. Japan's role in this developmental process has been curious at best. Although Japan claims victimization by the NAFTA, it continues with predatory trade practices in Southeast Asia. It appears that the rules change to the advantage of Japan.

From Japan's economic behavior (economic patterns and relationships) it can be determined that two of my hypotheses are supported. The first is that Japan's interest in Latin America stems from basic economic needs. This is suggested by the economic drive for raw materials and resources from the Latin American region that is supported by the country studies. One of the basic elements of economics is to move capital from the location of surplus to the location of deficit. Therefore, it can be said that Japanese basic economic requirements were the impetus for Southeast Asia and Latin American economic development.

The second is that Japan's interest in Latin America is geostrategically motivated. This is supported by several factors discussed in the economic analysis of Chapters III and IV:

1. The main premise of Japan's foreign policy is the dependence on economic strength. Japan has the intense desire to have a global bargaining power. Japan uses "monetary muscle" to influence politics such as in Mexico, Chile and Peru.

2. Japan has a fear of a Western Hemisphere trading bloc "lock-out"; thereby, causing a shrinkage in world trade which would significantly hurt Japan's economic security. Japan is maneuvering to outflank this perceived "lock-out" by solidifying substantial trade positions and economic influence in targeted Latin American countries. After all, it is enticing that the Americas control 21.69% of world trade in merchandise.

3. Japan wants to be taken seriously. The only way Japan knows how to get international recognition is to use economic clout to achieve political ends. What the Japanese exhibit as economic prowess is often dwarfed by the lack of political finesse.

The implications of both the emergence of economic trading blocs and the new found mission for Japan in Latin America, are all positive from an economic point of view. The emergence of a Pan-Pacific trade arrangement opens up free trade in a multitude of directions with as many options. Free trade can only help in the economic growth and development of Latin America and contribute to a chain reaction of economic stimuli around the Pacific Rim.

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